



1-1-1995

# Business Associations and Professions

University of the Pacific; McGeorge School of Law

Follow this and additional works at: <https://scholarlycommons.pacific.edu/mlr>



Part of the [Legislation Commons](#)

## Recommended Citation

University of the Pacific; McGeorge School of Law, *Business Associations and Professions*, 26 PAC. L. J. 281 (1995).

Available at: <https://scholarlycommons.pacific.edu/mlr/vol26/iss2/18>

This Greensheet is brought to you for free and open access by the Journals and Law Reviews at Scholarly Commons. It has been accepted for inclusion in McGeorge Law Review by an authorized editor of Scholarly Commons. For more information, please contact [mgibney@pacific.edu](mailto:mgibney@pacific.edu).

# Business Associations and Professions

## Business Associations and Professions; advertising—lawyer referral services

Business and Professions Code §§ 6157.5, 6157.6, 6157.7 (repealed); §§ 6150, 6158, 6158.1, 6158.2, 6158.3, 6158.4, 6158.5, 6158.7 (new); §§ 6155, 6156, 6157, 6157.2 (amended).  
AB 3659 (Horchner); 1994 STAT. Ch. 711

Existing law regulating lawyer referral services requires the California State Bar, on approval of the Supreme Court, to formulate and enforce rules and regulations governing these services.<sup>1</sup> Chapter 711 provides that application and renewal fees, required under existing law, be determined by considering certain factors while limiting the amount of those fees to the lesser of \$10,000 or one percent of the service's gross annual revenues.<sup>2</sup> Chapter 711 additionally requires lawyer referral services to separately serve those with limited financial resources.<sup>3</sup> Failure of a lawyer referral service to comply with the requirements delineated in Chapter 711 may result in the refusal or revocation of certification.<sup>4</sup> Chapter 711 further provides that any person engaged in unfair competition or false advertising, or that violates the provisions governing lawyer referral services, is liable for a specified civil penalty.<sup>5</sup>

Existing law prohibits the dissemination of advertisements using impersonations of the attorney or client, or dramatizations of events without disclosure that they are impersonations or dramatizations.<sup>6</sup> Chapter 711 adds to these pro-

---

1. CAL. BUS. & PROF. CODE § 6155 (amended by Chapter 711); *see id.* § 6155(f)(4) (governing lawyer referral services and requiring formulation and enforcement, by the California State Bar, of rules requiring lawyer referral services to pay application and renewal fees for certification).

2. *Id.* § 6155(f)(4) (amended by Chapter 711); *see id.* (listing the factors for consideration in certifying lawyer referral services including: (1) The service's gross annual revenues; (2) the number of panels composed of subscribing lawyers; (3) the number of panel members; (4) the amount of fees billed to panel members; and (5) the service's profit or nonprofit status).

3. *Id.* § 6155(f)(5) (amended by Chapter 711); *see id.* (providing that the California State Bar must require lawyer referral services to conduct ongoing activities aimed at increasing access to the justice system for those of limited means).

4. *Id.* § 6155(g) (amended by Chapter 711); *see id.* (listing the offenses constituting cause for denial of certification, including: (1) Noncompliance with the laws governing lawyer referral services; (2) conducting joint ventures with any entity that provides referrals to licensed or unlicensed health care providers; (3) consideration regarding referrals between lawyer referral services and health care professionals; and (4) advertising on behalf of lawyers in violation of the California Rules of Professional Conduct or the California Business and Professions Code).

5. *Id.* § 6156(a) (amended by Chapter 711); *see id.* (providing for a civil penalty defined in California Business and Professions Code §§ 17206, 17206.1, and 17536); *see also id.* § 17206 (West Supp. 1994) (establishing a civil penalty of up to \$2500 per engagement in unfair competition as defined in California Business and Professions Code § 17200); *id.* § 17206.1 (West Supp. 1994) (establishing a civil penalty of up to \$2500 per incident of false advertisement as defined in California Business and Professions Code § 17500); *id.* § 17536 (West Supp. 1994) (establishing a civil penalty of up to \$2500 per violation of California Business and Professions Code § 6155).

6. *Id.* § 6157.2 (amended by Chapter 711).

visions new requirements and prohibitions regarding attorney advertising in the electronic media.<sup>7</sup> Under Chapter 711, a spokesperson may be used so long as there is no direct or implicit assertion that he or she is a lawyer and there is a disclosure of the spokesperson's hired status.<sup>8</sup>

Under existing law, attorneys<sup>9</sup> are prohibited from publishing advertisements<sup>10</sup> that contain false, misleading, or deceptive language, or certain other statutorily proscribed statements.<sup>11</sup> Chapter 711 states that an advertisement is not false, misleading, or deceptive if it does not, as a whole, possess those characteristics and it is factually substantiated.<sup>12</sup> However, there is now a rebuttable presumption

---

7. *Id.* §§ 6158-6158.7 (enacted by Chapter 711); *see also id.* § 6157(d) (enacted by Chapter 711) (defining electronic medium as television or radio).

8. *Id.* § 6157.2(c) (amended by Chapter 711).

9. *See id.* § 6157(a) (amended by Chapter 711) (defining an attorney as a member in good standing of the California State Bar as well as his or her agent or law firm, or a corporation doing business within the state); *see also id.* § 6158.5 (enacted by Chapter 711) (including within the scope of AB 3639 all lawyers, members, law partnerships, law corporations, cooperatives, or other individuals or groups advertising the availability of legal services, while excluding qualified legal services projects defined in California Business and Professions Code Article 14 (commencing with § 6210) and nonprofit lawyer referral services).

10. *See id.* § 6157(c) (amended by Chapter 711) (defining an advertisement as any electronic or printed communication directed generally to the public rather than to a specific person and that solicits employment of legal services provided by the advertising attorney and is paid for by that attorney or by another on his or her behalf).

11. *Id.* § 6157.1 (West Supp. 1994); *see id.* § 6157.2(a)-(d) (amended by Chapter 711) (proscribing guarantees or warranties regarding the results of legal matters or representation by the attorney, assertions that the attorney can obtain immediate cash or quick settlements, impersonations of the attorney or clients or other dramatizations made without disclosure in the advertisement, and statements offering representation on a contingent basis unless accompanied by a statement that the client will be responsible for any costs incurred by the attorney when no recovery on behalf of the client is obtained); *see also* CAL. BUS. & PROF. CODE. § 6158.2 (enacted by Chapter 711) (providing a list of information presumed to be in compliance with Chapter 711 including the following: names, addresses, telephone numbers, and professional designations of the attorney and his or her firm and associates; fields of practice or specialization; fees for routine services within statutory limits; date and place of birth; date and place of admission to the bar; schools attended with dates of graduation, degrees earned, and other scholastic achievements; public or quasi-public offices held; military record; legal authorship; legal teaching positions; memberships and offices in legal organizations; technical and professional licenses; and memberships in scientific, technical, and professional organizations); MODEL RULES OF PROFESSIONAL CONDUCT Rule 7.1 (1983) (proscribing the making, by lawyers, of false or misleading communications regarding services); Eric L. Graves, Review of Selected 1993 California Legislation, *Business Associations and Professions: Advertising by Attorneys*, 25 PAC. L.J. 368, 407 (1994) (citing existing law relevant to attorney advertising).

12. CAL. BUS. & PROF. CODE § 6158 (enacted by Chapter 711).

that an advertisement is false, misleading, or deceptive under certain circumstances.<sup>13</sup> Chapter 711 additionally provides a list of information that is presumed not to be misleading or deceptive.<sup>14</sup>

Chapter 711 additionally requires that certain disclosures be made depending upon the nature and content of the advertisements.<sup>15</sup> Chapter 711 allows electronic media advertisements that state the attorney's rates and billing method as well as other information, provided that all advertised claims are factually substantiated.<sup>16</sup> Chapter 711 also creates a procedure for investigating complaints filed with the California State Bar against its members and against certified lawyer referral services, and for civil enforcement.<sup>17</sup> Violations of Chapter 711 may result in civil liability of up to \$5000 for individual violations of the provisions pertaining to electronic media advertising, and actions may be brought either by the California State Bar or by any person residing in the State of California.<sup>18</sup>

#### COMMENT

Chapter 711 was introduced partly to halt the use of electronic media for "unseemly and distasteful" advertisements which some believe demean the legal profession and contribute to the declining public image of lawyers.<sup>19</sup> Sponsors of Chapter 711 also cite the need to prevent advertisements which would undermine the credibility of the civil justice system, as well as to protect consumers from the misleading effects of advertisements in an area where consumers lack sophistication.<sup>20</sup>

---

13. *Id.* § 6158.1 (enacted by Chapter 711); *see id.* (listing the circumstance under which there will be a presumption of falsity, misleading, or deception, including: (1) Out-of-context assertions regarding the results of specific cases without adequate information about the facts or law leading to the results; (2) depiction of injuries, accident scenes, or other injurious events giving rise to a claim; and (3) references to monetary recovery).

14. *Id.* § 6158.2 (enacted by Chapter 711); *see id.* (providing a list of messages that are presumed as a whole to be not false, misleading, or deceptive, including: (1) Name, address, and telephone number; (2) fields of practice; (3) fees for routine services; (4) date and place of birth; (5) date and place of admission to the bar; (6) schools attended; (7) offices held; (8) military service; (9) legal authorship; (10) legal teaching positions; (11) bar membership, offices, and committee assignments; (12) legal fraternities; (13) technical and professional licenses; and (14) memberships in other associations and societies).

15. *Id.* § 6158.3 (enacted by Chapter 711); *see id.* (providing that electronic media advertisements conveying messages portraying results in particular cases must state one of two disclosures: (1) The factual and legal circumstances that justified the result portrayed in the message, including the basis for liability and the nature of the injury or damage, and (2) a statement that the result portrayed was dependent on the particular facts of that case and that actual results based on different facts will differ).

16. *Id.* § 6158 (enacted by Chapter 711); *see also* MODEL RULES OF PROFESSIONAL CONDUCT Rule 7.1(c) (1983) (providing that comparisons made by attorneys must be substantiated).

17. *Id.* § 6158.4 (enacted by Chapter 711).

18. *Id.* § 6158.4(e) (enacted by Chapter 711).

19. ASSEMBLY JUDICIARY COMMITTEE, COMMITTEE ANALYSIS OF AB 3659, at 3 (May 11, 1994).

20. *Id.*, at 3-4; *see id.* (asserting that the perception of attorneys as carnival barkers may lead consumers to believe that justice may be bought, sold, and traded like a commodity); *see also* Bill Ainsworth, *Bill to Limit TV, Radio Ads Passes Committee*, THE RECORDER, May 12, 1994, at 1 (citing the California Trial Lawyers

Those opposing Chapter 711 argue that unrestricted attorney advertising promotes consumer interests by increasing the availability of legal services to the public while reducing their cost.<sup>21</sup> Proponents, however, argue that contingency fees and other expenses result in lower net recovery by victims.<sup>22</sup>

Chapter 711 may face First Amendment challenges.<sup>23</sup> Complete prohibitions of attorney advertising have been held in violation of the First Amendment's Free Speech Clause,<sup>24</sup> however, restrictions which do not rise to the level of complete bans on attorney advertising have been held constitutional where they serve to advance a substantial state interest.<sup>25</sup> Nevertheless, the United States Supreme Court in *Zauderer v. Office of Disciplinary Counsel*,<sup>26</sup> emphasized that unjustified or unduly burdensome disclosure requirements might offend the First Amendment by chilling constitutionally protected commercial speech.<sup>27</sup>

The Supreme Court has held that advertising may be prohibited entirely where its particular form or method is inherently likely to deceive or has, in fact, been

---

Association's (CTLA) assertion of the need to protect consumers); John F. Wagner Jr., Annotation, *Restrictions on Attorneys' Advertisements Regarding Legal Services as Violating Federal Constitution's First Amendment—Supreme Court Cases*, 110 L. Ed. 2d 688, 694 (1993) (citing *Bates v. State Bar of Ariz.*, 433 U.S. 350, 383 (1977), as stating that misstatements that might be overlooked or deemed unimportant in other forms of advertising might be inappropriate in a legal context due to the public's lack of sophistication concerning legal services). *But see Bates*, 433 U.S. at 374-75 (stating that the lack-of-sophistication argument underestimates the public, that any common misconceptions should be remedied with more rather than fewer disclosures, and that the State Bar should bear the responsibility for creating an informed populace).

21. ASSEMBLY JUDICIARY COMMITTEE, COMMITTEE ANALYSIS OF AB 3659, at 4 (May 11, 1994); see *Consumers and Lawyers Against Censorship: Proposal to Restrict Political Ads Makes Plain Flaws in AB 3659*, PR Newswire, May 19, 1994, available in LEXIS, News Library, Cumwts File (asserting that attorney advertisements tend to increase competition and lead to lower prices for legal services as well as improve the flow of information to the elderly, low-income groups, and ethnic minorities who often find a lawyer through TV and radio advertisements); Terry Calvani et al., *Attorney Advertising and Competition at the Bar*, 41 VAND. L. REV. 761, 781 (1988) (arguing that attorney advertising allows reduced production costs, which lower prices without a corresponding reduction in quality (citing Timothy Muris & Fred McChesney, *The Effect of Advertising on the Quality of Legal Services*, 65 A.B.A. J. 1503, 1506 (1979))).

22. Stephen Hayward & K.L. Billingsley, Pacific Research Institute for Public Policy, *Lawyer Advertising in California: Estimates & Issues* (1994) (copy on file with the *Pacific Law Journal*); see *id.* at 10 (citing a 1989 study of 47,000 automobile accident victims who filed injury claims which found that lawyers drive up out-of-court settlement costs but yield less total cash to clients).

23. Claire Cooper, *Bill Would Tone Down Attorney Ads*, SACRAMENTO BEE, May 11, 1994, at A4; see *id.* (reporting opponents' predictions that AB 3659 will encounter serious First Amendment problems). *But see id.* (reporting the opposite conclusion drawn by proponents who cite Iowa's similar law, Iowa Court Rule DR 2-101, and its survival of state and federal challenges).

24. U.S. CONST. amend. I.

25. *In re R.M.J.*, 455 U.S. at 203 (supporting of the proposition that some restrictions on attorney advertising are constitutional (citing *Central Hudson Gas and Elec. Corp. v. Public Serv. Comm.*, 447 U.S. 557, 563-64 (1980))); see also *Zauderer*, 471 U.S. at 636 (holding that an attorney's rights to advertise are adequately protected provided disclosure requirements are reasonably related to the state's interest in preventing deception of consumers).

26. 471 U.S. 626 (1985).

27. *Zauderer*, 471 U.S. at 651; see *Central Hudson*, 447 U.S. at 561-62 (defining commercial speech as expression related solely to the economic interests of the speaker and his or her audience, and speech proposing a commercial transaction).

deceptive.<sup>28</sup> Thus attorney advertisements may still be prevented where they are false, deceptive, or misleading.<sup>29</sup>

Despite expected constitutional challenges to Chapter 711, similar laws restricting attorney advertising have survived in other states.<sup>30</sup> The Iowa Supreme Court has upheld a comprehensive regulatory scheme pertaining to attorney advertising in the electronic media in *Committee on Professional Ethics and Conduct of the Iowa State Bar v. Humphrey*.<sup>31</sup> In *Humphrey*, the court interpreted the special problems with electronic advertising referenced in *Bates v. State Bar of Arizona*<sup>32</sup> as warranting a special rule to regulate attorney advertising in the electronic media.<sup>33</sup> The *Humphrey* court cited a "very real potential for abuse" as satisfying the substantial-state-interest test<sup>34</sup> due to several factors differentiating electronic advertisement from other forms of advertisement.<sup>35</sup> The United States Supreme Court denied rehearing of *Humphrey*,<sup>36</sup> which upheld a restriction on attorney advertising that is essentially identical to that of Chapter 711.<sup>37</sup> The Supreme Court of New Jersey upheld similar restrictions on television advertising in *In re Petition of Felmeister & Isaacs*,<sup>38</sup> where the court ruled that the public

---

28. *In re R.M.J.*, 455 U.S. at 202; *see id.* (interpreting *Bates* and subsequent cases as holding that regulation and disciplinary actions are permissible where the particular advertisement is inherently likely to deceive or where the record indicates that a particular form or method of advertising has actually been deceptive); *Ohralik v. Ohio State Bar Ass'n*, 436 U.S. 447, 462 (1978) (holding that deceptive advertisements may be regulated and disciplinary action taken against their creators); *see also id.* (interpreting *Ohralik* as allowing complete prohibition of a type of advertising containing a high possibility of fraud, undue influence, intimidation, overreaching, and other forms of "vexatious conduct"); *id.* (citing *Friedman v. Rogers*, 440 U.S. 1, 10 (1979), as an example of a constitutionally permissible prohibition of a certain kind of advertising which had a history of working deception and abuse upon consumers).

29. *Zauderer*, 471 U.S. at 638.

30. IOWA CT. R. DR 2-101 (West 1994); N.J. CT. R. RPC 7.2 (West 1994); *see also* MODEL CODE OF PROFESSIONAL RESPONSIBILITY DR 2-101 (1994) (containing provisions similar to Chapter 711 enacted by Iowa, New Jersey, and several other states).

31. 377 N.W.2d 643, 646 (Iowa 1985), *reh'g denied*, 476 U.S. 1114 (1986).

32. 433 U.S. 350 (1977); *see id.* at 384 (stating that the special problems of advertising in the electronic media warrant special consideration when evaluating restrictions on the time, place, and manner of advertising).

33. *Humphrey*, 377 N.W.2d at 646.

34. *See supra* note 25 and accompanying text (discussing cases expounding the substantial-state-interest test).

35. *Humphrey*, 377 N.W.2d at 646; *see id.* (listing special problems regarding electronic media advertising including fleeting images which afford the recipient less opportunity for thoughtful consideration).

36. *Committee on Professional Ethics & Conduct of Iowa State Bar v. Humphrey*, 476 U.S. 1114 (1986).

37. ASSEMBLY JUDICIARY COMMITTEE, COMMITTEE ANALYSIS OF AB 3659, at 4 (May 11, 1994); *see id.* (citing the CTLA's assertion that, because AB 3659 contains the same language of the Iowa law upheld in *Humphrey*, attorney advertising in California's electronic media will also be found to present special problems that warrant special consideration within the meaning of *Bates*); *see also Humphrey*, 377 N.W.2d at 655 (describing the Iowa law at issue in that case as limiting advertising to words and numbers only, articulated by a single nondramatic voice, not that of the lawyer, and with no other background sound).

38. 518 A.2d 188 (N.J. 1986).

interest would be better served by a requirement that attorney advertisements be "predominantly informational."<sup>39</sup>

Regardless of the predicted legal challenges, Chapter 711 will likely survive constitutional scrutiny as have other similar statutes throughout the country.<sup>40</sup>

*Mark W. Owens*

## **Business Associations and Professions; advocating appropriate health care—practitioners**

Business and Professions Code § 510 (new); § 2056 (amended).  
AB 3390 (B. Friedman); 1994 STAT. Ch. 1119

Existing law declares that it is the public policy<sup>1</sup> of the State that physicians and surgeons be encouraged to advocate for medically appropriate health care.<sup>2</sup> Chapter 1119 adds similar provisions for all health care practitioners.<sup>3</sup>

---

39. *In re* Petition of Felmeister & Isaacs, 518 A.2d at 188-89 (N.J. 1986); *see id.* (upholding a prohibition on the use of drawings, animations, dramatization, music or lyrics in television advertising by attorneys); *see also id.* at 189 n.1 (defining predominantly informational communications as those which convey factual information that is predominantly and rationally related to a consumers' need for and choice of counsel).

40. *See supra* note 30-39 and accompanying text (discussing the success of similar attorney-advertising restrictions in other states).

---

1. *See* Safeway Stores Inc. v. Retail Clerks Int'l Ass'n, 41 Cal. 2d 567, 575, 261 P.2d 721, 726 (1953) (defining public policy as a principle of law preventing any person from harming the public or the public good, or undermining security in individual rights).

2. CAL. BUS. & PROF. CODE § 2056(b) (amended by Chapter 1119); *see id.* (defining "to advocate for medically appropriate health care" to mean to contest a payor's denial of payment for service or to protest a decision, policy, or practice that a physician reasonably believes impairs his or her ability to provide appropriate health care); *id.* § 2056(e) (amended by Chapter 1119) (providing that medically appropriate health care in a hospital is to be defined by the medical staff and approved by the governing body, as long as it is consistent with the learning and skill ordinarily possessed by reputable physicians practicing within the legal standard of care); *see also id.* § 2056(c) (amended by Chapter 1119) (providing that it is against public policy for any person to penalize, in any way, a physician for advocating for medically appropriate health care). *See generally* Ann P. Wathen, Review of Selected 1993 California Legislation, *Business Associations and Professions; Advocacy of Health Care*, 25 PAC. L.J. 368, 410 (1994) (describing California Business and Professions Code § 2056).

3. CAL. BUS. & PROF. CODE § 510 (enacted by Chapter 1119); *see id.* § 510(h) (enacted by Chapter 1119) (defining health care practitioner as a person who is described in California Business and Professions Code § 900(f) and who is either a licensee or someone granted appeal rights under a contract for health care services); *id.* § 805(a)(2) (West Supp. 1994) (defining licensee as a physician and surgeon, podiatrist, clinical psychologist, or dentist); *id.* § 900(f) (West 1990) (defining health care practitioner as any person who engages in acts which are the subject of licensure or regulation pursuant to the Healing Arts Division of the California Business and Professions Code); *see also* SENATE COMMITTEE ON BUSINESS AND PROFESSIONS, COMMITTEE ANALYSIS OF AB 3390, at 1 (June 27, 1994) (stating that AB 3390 gives all health care practitioners protection similar to that given to physicians who advocate for appropriate health care). *See generally* ASSEMBLY COMMITTEE ON HEALTH, COMMITTEE ANALYSIS OF AB 3390, at 2 (May 3, 1994) (comparing California

Chapter 1119 provides that it is the public policy of the State that a health care practitioner be encouraged to advocate for appropriate health care for his or her patients and that any decision by an entity<sup>4</sup> to penalize a health care practitioner for such advocacy violates public policy.<sup>5</sup> Chapter 1119 explicitly does not prohibit a payor from making the decision not to pay for a medical service or from enforcing peer or utilization review.<sup>6</sup> Further, Chapter 1119 does not prohibit disciplinary actions to be taken against health care providers by the governing body of a hospital or by a licensing authority.<sup>7</sup>

#### INTERPRETIVE COMMENT

Chapter 1119 was enacted to protect health care practitioners who advocate for appropriate health care for their patients pursuant to *Wickline v. State of California*.<sup>8</sup> The *Wickline* case was the first case where there was an attempt made to tie a health care payor into the chain of causation in a medical malpractice case.<sup>9</sup> In *Wickline*, the court found that the third party payor was not a party to the medical decision which allegedly resulted in harm to the patient and therefore could not be held liable for the results of that decision.<sup>10</sup> The third party payor, Medi-Cal, denied a physician's request to cover a portion of the patient's hospital stay.<sup>11</sup> The patient was then released from the hospital.<sup>12</sup> The patient claimed that

---

Business and Professions Code § 2056 relating to physicians with § 510 relating to health care practitioners).

4. See CAL. BUS. & PROF. CODE § 510(c) (enacted by Chapter 1119) (including individuals, partnerships, corporations or organization as an entity).

5. *Id.* § 510(b)-(c) (enacted by Chapter 1119); see *id.* § 510(e) (enacted by Chapter 1119) (providing that "appropriate health care" in a hospital setting is to be defined by the hospital medical staff and approved by the governing body consistent with that degree of learning and skill ordinarily possessed by reputable health care practitioners with the same license or certification and practicing according to the applicable legal standard of care). See generally Paul Cotton, *Determining More Good Than Harm is Not Easy*, 270 JAMA 153 (1993) (explaining that in medicine, the word "appropriate" is difficult to define and apply because of changing knowledge bases and conflicting scientific studies).

6. CAL. BUS. & PROF. CODE § 510(d) (enacted by Chapter 1119); see *id.* § 809.05 (West 1990) (mandating that licentiates conduct peer reviews); *id.* § 809.5(a) (West Supp. 1994) (authorizing a peer review committee to immediately suspend or restrict a licentiate's privileges where a patient's health is in imminent danger); CAL. INS. CODE § 791.10 (West 1993) (providing that the agent responsible for making a decision to deny payment on an insurance policy must make available the reasons for denial in writing and provide the policy holder with a summary of his or her rights); cf. CAL. BUS. & PROF. CODE § 2056(d) (amended by Chapter 1119) (providing that the law protecting physicians from advocating for appropriate medical care will not prevent a payor from deciding not to pay for a service or enforcing peer and utilization review).

7. CAL. BUS. & PROF. CODE § 510(f)-(g) (enacted by Chapter 1119); see *id.* § 510(i) (enacted by Chapter 1119) (stating that Chapter 1119 does not affect the scope of practice of any health care practitioner).

8. *Id.* § 510(a) (enacted by Chapter 1119); *Wickline v. State of California*, 192 Cal. App. 3d 1630, 239 Cal. Rptr. 810 (1986); see *Wilson v. Blue Cross of S. Cal.*, 222 Cal. App. 3d 660, 674, 271 Cal. Rptr. 876, 884 (1990) (refusing to apply *Wickline* dicta to grant summary judgment in a case where the claim was brought directly against an insurance company rather than a physician and there remained triable issues of fact relating to the patient's death). See generally SENATE COMMITTEE ON BUSINESS AND PROFESSIONS, COMMITTEE ANALYSIS OF AB 3390, at 2 (June 27, 1994) (describing complaints by health care practitioners that they have been terminated by health care providers as a result of challenges to utilization review decisions).

9. *Wickline*, 192 Cal. App. 3d at 1633, 239 Cal. Rptr. at 811.

10. *Id.* at 1646, 239 Cal. Rptr. at 819.

11. *Id.* at 1638, 239 Cal. Rptr. at 814.



the early release from the hospital resulted in complications leading to the amputation of her right leg.<sup>13</sup> The court stated that a physician may be held liable for third party payor decisions, when the physician has complied with a decision, without protest, which he or she believes to be erroneous.<sup>14</sup>

However, health care practitioners who followed the message of *Wickline* by protesting third party payor decisions found that their contracts with those providers were often terminated.<sup>15</sup> Practitioners who fought this wrongful discharge would have no legal remedy because the public policy they relied on was not codified.<sup>16</sup>

Chapter 1119 codifies the public policy that a health care practitioner advocate for appropriate health care and that it is against public policy for a third party payor to terminate business relations with the practitioner based solely on such patient advocacy.<sup>17</sup>

*Bonnie M. George*

## **Business Associations and Professions; alcoholic beverages—sale to nonprofit organizations**

Business and Professions Code § 25503.9 (amended).  
AB 2919 (Frazee); 1994 STAT. Ch. 266

---

12. *Id.* at 1639, 239 Cal. Rptr. at 815.

13. *Id.* at 1633, 239 Cal. Rptr. at 811.

14. *Id.* at 1645, 239 Cal. Rptr. at 819.

15. See ASSEMBLY COMMITTEE ON HEALTH, COMMITTEE ANALYSIS OF AB 3390, at 2 (May 3, 1994) (stating that the California Psychological Association has received complaints from health care practitioners terminated by third party payors as the result of challenges to payment decisions made on behalf of patients).

16. See *Gantt v. Sentry Insurance*, 1 Cal. 4th 1083, 1095, 824 P.2d 680, 688, 4 Cal. Rptr. 2d 874, 881 (1992) (holding that, in wrongful discharge actions, courts may not declare public policy violations without a basis in either constitutional or statutory provisions); ASSEMBLY COMMITTEE ON HEALTH, COMMITTEE ANALYSIS OF AB 3390, at 3 (May 3, 1994) (stating that Chapter 1119 is intended to codify public policy in order to provide a basis for wrongful discharge actions). See generally Laurie A. Erdman, Note, *Gantt v. Sentry Insurance: When Can an Employee be Discharged? Ask the Legislature*, 25 PAC. L.J. 107 (1993) (discussing *Gantt v. Sentry Insurance*).

17. CAL. BUS. & PROF. CODE § 510(b)-(c) (enacted by Chapter 1119).

---

Existing law allows winegrowers<sup>1</sup> and beer manufacturers<sup>2</sup> to give or sell their products to nonprofit organizations<sup>3</sup> at prices other than those contained in schedules<sup>4</sup> required to be filed with the Department of Alcoholic Beverage Control.<sup>5</sup>

Chapter 266 extends this exemption to licensed beer or wine importers<sup>6</sup> selling their products to nonprofit organizations at prices other than those filed in accordance with the Alcoholic Beverage Control Act.<sup>7</sup>

#### INTERPRETIVE COMMENT

Chapter 266 was enacted primarily to permit wine importers as well as growers and beer manufacturers to furnish their products to winetastings and festivals sponsored by private nonprofit organizations.<sup>8</sup> Chapter 266 allows importers to provide alcoholic beverages to nonprofit organizations for free or at a reduced

---

1. See CAL. BUS. & PROF. CODE § 23013 (West 1985) (defining winegrower as any person with the equipment for converting grapes into wine engaged in the production of wine except for persons producing 200 gallons or less per year for solely personal consumption).

2. See *id.* § 23012 (West 1985) (defining beer manufacturer as any person engaged in the manufacture of beer).

3. See CAL. REV. & TAX. CODE §§ 23701a, 23701d, 23701e, 23701f, 23701r (West 1992 & Supp. 1994) (defining the types of nonprofit organizations within the scope of AB 2919 including charitable corporations; trade associations; labor, agricultural, or horticultural organizations; religious, scientific, testing for public safety, literary, educational, amateur or humanitarian corporations; business leagues, chambers of commerce, real estate boards, and boards of trade under certain conditions; social welfare and employees' organizations and civic leagues under certain conditions; and political organizations under certain conditions).

4. See CAL. BUS. & PROF. CODE § 25000 (West Supp. 1994) (requiring manufacturers, importers, and wholesalers of beer to file written schedules of selling prices charged); see also *id.* § 24750.5 (West 1985) (authorizing fair trade contracts for wine).

5. *Id.* § 25503.9 (amended by Chapter 266); see *id.* § 23050 (West 1985) (establishing the Department of Alcoholic Beverage Control); see also CAL. CONST. art. XX, § 22 (defining the powers and composition of the Department of Alcoholic Beverage Control).

6. See CAL. BUS. & PROF. CODE § 23017 (West 1985) (defining importer as any consignee of alcoholic beverages for delivery or use within California, any person other than a public warehouse, taking first delivery of alcoholic beverages brought from outside the state, any person licensed as an importer, or any person bringing alcoholic beverages into the state for delivery or use within the state); see also *id.* § 23004 (West 1985) (defining alcoholic beverage as including alcohol, spirits, liquor, wine, beer, and every liquid or solid containing one half of one percent or greater of the same ingredients); 3 CAL. JUR., *Alcoholic Beverages* § 1 (Bancroft-Whitney, 3d ed. 1973) (defining distilled spirits, beer, and wine).

7. CAL. BUS. & PROF. CODE § 25503.9 (amended by Chapter 266); see ASSEMBLY FLOOR, COMMITTEE ANALYSIS OF AB 2919, at 1 (Apr. 21, 1994) (stating that AB 2919 allows sales or donations of alcohol to nonprofit organizations at prices other than those filed with the Department of Alcoholic Beverage Control).

8. *Calendar*, THE RECORDER, Feb. 22, 1994, at 18.

cost.<sup>9</sup> Thus, Chapter 266 addresses an oversight in earlier legislation which failed to remedy the restricted use of alcoholic beverages at fundraising events.<sup>10</sup>

*Mark W. Owens*

## **Business Associations and Professions; attorney discipline—right to exculpatory evidence**

Business and Professions Code § 6085 (amended).  
AB 2928 (Horcher); 1994 STAT. Ch. 190

Existing law governing disciplinary actions against attorneys affords charged lawyers certain rights, including the right to receive notice of the charges against them, to defend themselves by introduction of evidence, to be represented by counsel, to examine and cross-examine witnesses, and to issue subpoenas.<sup>1</sup> Chapter 190 adds to this list the right to receive any exculpatory evidence possessed by the State Bar following the initiation of a disciplinary proceeding and any evidence which becomes available thereafter.<sup>2</sup>

### **INTERPRETIVE COMMENT**

Chapter 190 was enacted to address complaints by California attorneys that the existing disciplinary system enforced by the State Bar too severely sanctions the state's lawyers.<sup>3</sup> Chapter 190 was intended to reduce the number of questionable

---

9. CAL. BUS. & PROF. CODE § 25503.9 (amended by Chapter 266); cf. SENATE FLOOR, COMMITTEE ANALYSIS OF AB 1666, at 2 (Aug. 16, 1993) (stating the purpose of a similar amendment to California Business and Professions Code § 25503.9, during the 1993-1994 California Legislature Regular Session (AB 1666), as facilitating donations or reduced-cost sales of alcoholic beverages to charitable or nonprofit organizations).

10. Telephone Interview with George Wiley, Legislative Consultant for the Senate Governmental Organizations Committee (June 13, 1994) (copy on file with the *Pacific Law Journal*); see also SENATE FLOOR, COMMITTEE ANALYSIS OF AB 1666, at 2 (Aug. 16, 1993) (citing the current law as too restrictive regarding the number and types of non-profit organizations able to supply free alcoholic beverages).

---

1. CAL. BUS. & PROF. CODE § 6085 (amended by Chapter 190); see *Giddens v. State Bar*, 28 Cal. 3d 730, 735, 170 Cal. Rptr. 812, 815 (1981) (interpreting California Business and Professions Code § 6085 to afford attorney defendants the right to a fair hearing which can only be provided by allowing them the opportunity to cross-examine witnesses, obtain and proffer evidence in their own defense, subpoena witnesses on their own behalf, or offer any other evidence which might mitigate the charges). See generally CAL. BUS. & PROF. CODE §§ 6090-6095 (West 1990 & Supp. 1994) (governing attorney disciplinary actions).

2. CAL. BUS. & PROF. CODE § 6085(b) (amended by Chapter 190); see *id.* (granting attorneys the right to receive exculpatory evidence at the inception of the investigation or as soon as it is discovered and no less than 15 days before the hearing).

3. ASSEMBLY JUDICIARY COMMITTEE, COMMITTEE ANALYSIS OF AB 2928, at 2 (Mar. 23, 1994); see Scott Harris, *Willie Brown's Plan to Ease the Pain of Lawyers*, L.A. TIMES, July 15, 1993, at B2 (reporting concerns that under the State Bar's system more than 100 attorneys per year have been either disbarred or

convictions of attorneys in disciplinary actions in a system which previously did not require disclosure of exculpatory evidence.<sup>4</sup>

Under Chapter 190, attorneys will be afforded the same rights given criminal defendants and attorneys in other states to have access to potentially exonerating evidence possessed by prosecutors.<sup>5</sup> Thus Chapter 190 was intended to promote fairness and justice in the prosecution of attorney disciplinary actions.<sup>6</sup>

*Mark W. Owens*

## **Business Associations and Professions; contractors—Disaster Fraud Protection Act of 1994**

Business and Professions Code §§ 7158, 7159, 7161 (amended); Penal Code § 667.16 (new).  
SB 634 (Craven); 1994 STAT. Ch. 362  
(Effective July 9, 1994)

Existing law defines certain actions by contractors<sup>1</sup> or others involved in performing building repairs in connection with improvement contracts as misdemeanors, including falsely representing an improvement contract as com-

---

forced to resign under pressure).

4. SENATE JUDICIARY COMMITTEE, COMMITTEE ANALYSIS OF AB 2928, at 2 (June 14, 1994).

5. *Id.*; see Thomas M. Fleming, Annotation, *Liability of Police or Peace Officers for False Arrest, Imprisonment, or Malicious Prosecution as Affected by Claim of Suppression, Failure to Disclose, or Failure to Investigate Exculpatory Evidence*, 81 A.L.R. 4TH 1031, 1053 (1993) (discussing cases in which law enforcement officers and their employers were held liable for false imprisonment or malicious prosecution where exculpatory evidence was concealed or not disclosed); see also CAL. PENAL CODE § 1054.1(e) (West Supp. 1994) (requiring prosecuting attorneys to disclose to the defendant or his or her counsel any exculpatory evidence known to the prosecutor); IOWA CR. R. DR 7-103 (West 1995) (requiring timely disclosure of exculpatory evidence by public prosecutors or other government lawyers); KAN. S. CT. R. 225 (West 1987) (requiring a public prosecutor or other government lawyer in an attorney disciplinary action to disclose any evidence that would tend to negate the guilt of the accused); Committee on Prof. Ethics & Conduct v. Ramey, 512 N.W.2d 569, 572 (Iowa 1994) (applying Iowa Rules of Court DR 7-103 in the context of an attorney disciplinary action and holding that the prosecutor must disclose exculpatory evidence); State Bar v. Claiborne, 756 P.2d 464, 507 (Nev. 1988) (applying to the context of an attorney disciplinary proceeding, the rule in Brady v. Maryland, 373 U.S. 83, 91 (1963) which requires disclosure of exculpatory evidence to comply with constitutional due process requirements). *But compare* Fleming, *supra*, at 1053 (citing instances where nondisclosure of exculpatory evidence resulted in findings of malicious prosecution) with Stanwyck v. Horne, 146 Cal. App. 3d 450, 461-62, 194 Cal. Rptr. 228, 235-36 (1983) (holding that, although members of the bar may sometimes be subject to fraudulent complaints, jurisdictions have an absolute privilege regarding disciplinary proceedings) and 5 B.E. WITKIN, SUMMARY OF CALIFORNIA LAW, *Torts* § 457 (9th ed. 1988) (citing California cases where State Bar disciplinary proceedings did not constitute instances of malicious institution of administrative proceedings).

6. ASSEMBLY JUDICIARY COMMITTEE, COMMITTEE ANALYSIS OF AB 2928, at 2 (Mar. 23, 1994).

---

1. See CAL. BUS. & PROF. CODE § 7026 (West Supp. 1994) (defining contractor).

plete for purposes of obtaining payment or credit, failing to comply with various requirements for home improvement contracts,<sup>2</sup> engaging in fraudulent practices, using false or deceptive advertising, or making substantial misrepresentations.<sup>3</sup> Under existing law, the maximum penalty available for such violations is \$5000 and/or a maximum jail sentence of one year.<sup>4</sup> Under Chapter 362, if these prohibited acts are committed with the plan or scheme of defrauding a property owner in connection with repairing a structure damaged in a natural disaster,<sup>5</sup> the maximum allowable penalty is increased to \$25,000.<sup>6</sup> Additionally, Chapter 362

---

2. See *id.* § 7151.2 (West Supp. 1994) (defining home improvement contracts).

3. *Id.* §§ 7158, 7159, 7161 (amended by Chapter 362); see *id.* § 7158(a) (amended by Chapter 362) (providing that accepting or receiving a document which evidences completion of performance of an improvement contract with knowledge of its falsity and using it for purposes of receiving payment or credit is a misdemeanor); *id.* § 7159 (amended by Chapter 362) (requiring every home improvement contract to be evidenced by a writing that will include, *inter alia*, the name and license number of the contractor, the expected completion date of the work, a drawing of the work to be completed, and a schedule of payments); *id.* § 7161(a),(c) (amended by Chapter 362) (providing that it is a misdemeanor to, *inter alia*, use false, misleading, or deceptive advertising as a means of inducing individuals to enter into improvement contracts, to make any substantial misrepresentations, and to engage in fraud in executing a contract); see also *Asdourian v. Araj*, 38 Cal. 3d 276, 282-83, 696 P.2d 95, 99, 211 Cal. Rptr. 703, 706 (1985) (holding that the Contractors' State Licensing Law does not have to be literally complied with when the party who seeks to escape his obligation has received the full protection that the statute contemplates); *Elliott v. Contractors' State License Bd.*, 224 Cal. App. 3d 1048, 1051, 274 Cal. Rptr. 286, 288 (1990) (stating that a failure to provide a homeowner with a property home improvement contract constitutes a violation of California Business and Professions Code § 7159); *id.* at 1051, 274 Cal. Rptr. at 288 (1990) (stating that a flier which advertised the services of a contractor and provided an incorrect license number constitutes false advertising in violation of California Business and Professions Code § 7161); *Davenport & Co. v. Spieker*, 197 Cal. App. 3d 566, 570, 242 Cal. Rptr. 911, 914 (1988) (allowing a contractor to recover for work performed pursuant to an oral modification of a written contract, and stating that the public policy interest underlying California Business and Professions Code § 7159 is not contravened by allowing enforcement of an oral contract since the consumer was not a member of a group of unsophisticated consumers that California Business and Professions Code § 7159 is intended to protect); *West v. State*, 181 Cal. App. 3d 753, 758-59, 227 Cal. Rptr. 16, 18 (1986) (concluding that fraudulently representing that the plaintiffs must first pay the full contract price to be placed in a trust account and to be used as needed was a violation of California Business and Professions Code § 7159); *Hope v. Contractors' State License Bd.*, 228 Cal. App. 2d 414, 418-19, 39 Cal. Rptr. 514, 517 (1964) (stating that the California Contractors' License Law, including California Business and Professions Code § 7158, was enacted for the safety and the protection of the public against persons inexperienced in contracting work); See generally SENATE FLOOR, COMMITTEE ANALYSIS OF SB 634, at 2 (June 9, 1994) (stating that although misrepresentation is a common allegation, such a claim is difficult to substantiate; as a result, most cases are based upon a lack of a written contract or requiring an excessive deposit).

4. CAL. BUS. & PROF. CODE §§ 7158(a), 7159, 7161 (amended by Chapter 362).

5. See *id.* §§ 7158(b), 7159(n), 7161(f) (amended by Chapter 362) (providing that in order for these provisions to be applicable, the natural disaster must result in either the Governor proclaiming a state of emergency pursuant to Government Code § 8625 or the President proclaiming an emergency or major disaster); CAL. GOV'T CODE § 8558 (West 1992) (defining different degrees of emergency, including state of war emergency, state of emergency, and local emergency); *id.* § 8625 (West 1992) (providing that the Governor can proclaim a state of emergency when circumstances described in Government Code § 8558 occur, when requested to do so by a city mayor or chief executive or by a county chairman of the board or administrative officer, or when the Governor finds that local authority is inadequate to cope with the emergency). See generally Joan Conrow, *Picking up the Pieces*, HAW. INVESTOR, Dec. 1992, at 10 (reporting that individuals from the construction industry have stated that there is little indication that any contractors are defrauding people as a result of damage caused by Hurricane Iniki in Hawaii).

6. CAL. BUS. & PROF. CODE §§ 7158(b), 7159(n), 7161(f) (amended by Chapter 362); cf. Victoria White, *County Cracks Down on Price Gouging*, ST. PETERSBURG TIMES, Mar. 20, 1993, at 1 (stating that the Crystal River City Council, in response to the disastrous floods, approved an anti-price-gouging ordinance that

mandates that the individual convicted make full restitution to the victim, subject to the individual's ability to pay.<sup>7</sup>

Existing law classifies forgery,<sup>8</sup> grand theft,<sup>9</sup> and false pretenses<sup>10</sup> as felony violations.<sup>11</sup> Chapter 362 mandates that a one-year enhancement be imposed in addition and consecutive to the penalty prescribed for conviction if the felony was committed as part of a plan or scheme to defraud an owner of a structure in connection with making repairs resulting from damage sustained in a natural disaster.<sup>12</sup> Chapter 362 further provides the courts with an element of discretion, providing that the additional penalty can be eliminated if mitigating circumstances warrant.<sup>13</sup>

#### INTERPRETIVE COMMENT

Chapter 362 was enacted to deter persons from engaging in acts of fraud in connection with contracts to repair structures damaged in earthquakes.<sup>14</sup> Because of the tremendous destruction typically caused by natural disasters and because of the restoration process required in their aftermath, property owners who are the

---

makes it a criminal offense to raise prices for food, medicine, fuel, or building supplies more than five percent above the price listed the day before the floods occurred); *cf. also* CAL. BUS. & PROF. CODE § 6788 (West Supp. 1994) (providing that a professional engineer who, *inter alia*, offers to practice engineering without legal authority, impersonates or uses the seal of another practitioner, or uses an expired or revoked certificate in connection with repairing structures damaged by natural disasters for which a state of emergency is declared by the Governor or a major disaster declared by the President shall be punished by a fine of up to \$10,000 and/or imprisonment for 16 months, 2 years, or 3 years).

7. CAL. BUS. & PROF. CODE §§ 7158(b), 7159(n), 7161(f) (amended by Chapter 362); *see* CAL. PENAL CODE § 1203.1b(b) (West Supp. 1994) (providing a means for determining an individual's ability to pay).

8. *See* CAL. PENAL CODE § 470 (West 1988 & Supp. 1994) (defining forgery); *see also* *People v. McGlade*, 139 Cal. 66, 69, 72 P. 600, 601 (1903) (holding that a certain instrument or demand for payment for money due for labor performed can be the target of forgery).

9. *See* CAL. PENAL CODE § 487 (West 1988 & Supp. 1994) (defining grand theft as the taking of money, labor, or real or personal property taken exceeding \$400).

10. *See id.* § 532 (West Supp. 1994) (defining false pretenses); *see also* *People v. Layman*, 259 Cal. App. 2d 404, 408, 66 Cal. Rptr. 267, 269 (1968) (holding that the offense of taking property by false pretenses is not committed until the transaction creates an obligation).

11. CAL. PENAL CODE §§ 470, 487, 532 (West 1991 & Supp. 1994).

12. *Id.* § 667.16(a) (enacted by Chapter 362); *see id.* § 667.16(b) (enacted by Chapter 362) (limiting the section's applicability to natural disasters which result either in the Governor declaring a state of emergency or the President declaring an emergency or a major disaster); *supra* note 5 (discussing the definition of natural disaster and specifying the circumstances which warrant a declaration of a state of emergency). *But see* SENATE FLOOR, COMMITTEE ANALYSIS OF SB 634, at 2 (June 9, 1994) (stating that few violators actually serve jail time for such violations, with most being sentenced to community service).

13. CAL. PENAL CODE § 667.16(c) (enacted by Chapter 362); *see id.* (providing that the reasons for striking the additional punishment must be stated on the record).

14. ASSEMBLY FLOOR, COMMITTEE ANALYSIS OF SB 634, at 2 (May 17, 1994); *see id.* (stating that, in particular, this bill was intended as a response to complaints made by mobile home owners who were allegedly defrauded in regard to the reinstallation or repair of their mobilehomes subsequent to the Northridge earthquake). *But see* *Conrow*, *supra* note 5, at 10 (stating that contractors face a large upfront capital investment in order to assist owners of damaged structures and unless the state provides a pool of low-interest funds to assist contracting firms, it may be difficult for homeowners to employ licensed contractors for repair work); *id.* (stating that unlicensed contractors may become increasingly attractive to homeowners tired of waiting for repairs).

victims of natural disasters are a vulnerable target for fraudulent repair schemes.<sup>15</sup> Therefore, Chapter 362 provides these individuals with some protection from fraudulent practices of those with whom they contract for construction improvements or repairs as well as ensures that licensed business professionals adhere to ethical business practices.<sup>16</sup>

*Laura J. Fowler*

## **Business Associations and Professions; corporations—valuation of unlawful distributions**

Corporations Code §§ 316, 500, 502, 503, 506, 25116 (amended).  
AB 3649 (Weggeland); 1994 STAT. Ch. 1064

---

15. ASSEMBLY FLOOR, COMMITTEE ANALYSIS OF SB 634, at 2 (May 17, 1994); *see* Davenport & Co. v. Spieker, 197 Cal. App. 3d 566, 569, 242 Cal. Rptr. 911, 913 (1988) (stating that the public policy interest underlying California Business and Professions Code § 7159 is the protection of unsophisticated consumers); *see also* 42 U.S.C.A. §§ 7701-7706 (West 1983 & Supp. 1994) (setting forth the provisions of the Earthquake Hazards Reduction Act); Tina Daunt & Daryl Kelley, *Earthquake: The Long Road Back*, L.A. TIMES, Jan. 26, 1994, at B2 (discussing price gouging ordinances that have been passed by cities and counties, and giving examples of alleged instances of price gouging, including pieces of plywood worth \$8.00 being sold for \$200). *But see* SENATE FLOOR, COMMITTEE ANALYSIS OF SB 634, at 2 (May 17, 1994) (stating that although natural disasters may create a target-rich environment for fraud, the incidents of shady contractors preying on vulnerable homeowners has declined in recent years because of increasing efforts to educate the public at disaster assistance centers and because of increasing efforts to check a contractor's license at disaster related job sites); Conrow, *supra* note 5, at 10 (stating that Kauai residents appear to be better informed about their rights under the law because of their usage of a recently published newspaper insert that lists all licensed contractors).

16. *See* Elliott v. Contractors' State License Bd., 224 Cal. App. 3d 1048, 1055, 274 Cal. Rptr. 286, 291 (1990) (stating that the Contractors' State License Law codified in the California Business and Professions Code was enacted in order to protect the public against dishonesty and incompetence in the business of contracting); *see also* Hope v. Contractors' State License Bd., 228 Cal. App. 2d 414, 418-19, 39 Cal. Rptr. 514, 517 (1964) (stating the state contractor licensing statutes were enacted for the safety and protection of the public against imposition by persons inexperienced in contracting work and for prevention of fraudulent acts by contractors); CAL. CODE REGS. tit. 16, §§ 810-887 (1994) (setting forth the provisions of the Contractors' State Licensing Board); David E. Brady & Stephanie Stassel, *Quake Directory*, L.A. TIMES, Feb. 22, 1994, at B6 (providing important information for victims of the Northridge earthquake, including an Earthquake Fraud Hot Line and a phone number for purposes of reporting price-gouging, unlicensed contractors, charity scams, and fraud); Eric Malnic & John Hurst, *Quake Relief Efforts Picks Up, U.S. Promises \$283 Million More Aid to L.A.*, L.A. TIMES, Jan. 23, 1994, at A1 (discussing enforcement of a price-gouging ordinance passed by Los Angeles County after the Northridge Earthquake that bars merchants and contractors from raising prices more than 10% above pre-disaster levels); *cf.* MO. ANN. STAT. § 44.023.1 (Vernon 1992) (providing for the establishment of an emergency volunteer program, whereby architects, engineers, and contractors volunteer their services in the event of an earthquake or other natural disaster); Conrow, *supra* note 5, at 10 (describing the Iniki Rebuild Coalition, an organization formed by the construction industry and government organizations in order to educate and train the public and to familiarize workers with codes and building techniques after Hurricane Iniki in Hawaii).

Existing law provides that any shareholder<sup>1</sup> who receives an illegal distribution<sup>2</sup> with knowledge of the impropriety is liable to the corporation for the amount received plus accrued interest.<sup>3</sup> Existing law imposes analogous liability on the corporation's directors<sup>4</sup> who approve of any illegal distribution.<sup>5</sup> Existing law further requires that the approving directors be held jointly and severally liable<sup>6</sup> to the corporation.<sup>7</sup>

Chapter 1064 mandates that for purposes of assessing the civil liability of a shareholder who knowingly receives an illegal noncash distribution of corporate property and a director who approves such distribution, the value of the property is its fair market value at the time of the distribution plus interest from the date of distribution.<sup>8</sup>

Existing law authorizes a corporation to make distributions to its shareholders only when the corporation's assets exceed its liabilities by a specified ratio or the

---

1. See CAL. CORP. CODE § 185 (West 1990) (defining shareholder as one who is a holder of record of shares); see also *id.* § 184 (West 1990) (defining shares as units into which the proprietary interests in a corporation are divided in the articles).

2. See *id.* § 166 (West Supp. 1994) (defining distribution to its shareholders as the transfer of cash or property by a corporation to its shareholders without consideration, whether by way of dividend or otherwise, except a dividend in shares of the corporation, or the purchase or redemption of its shares for cash or property, including the transfer, purchase, or redemption by a subsidiary of the corporation).

3. *Id.* § 506(a) (amended by Chapter 1064); see *England v. Christensen*, 243 Cal.2d 413, 432, 52 Cal. Rptr. 402, 414 (1966) (ruling that where there was evidence that the corporate shareholders who sold their shares to the corporation engaged in the affairs and day-to-day conduct of the corporation's business, it could be inferred that they had the requisite knowledge of facts indicating the impropriety of the corporation's purchase of their shares); see also *Oilwell Chemical & Materials Co. v. Petroleum Supply Co.*, 64 Cal.2d 367, 373, 148 P.2d 720, 723 (1944) (holding that where dividends are regularly and legally declared by the board of directors of a solvent corporation and are rightfully paid out of profits, no action to recover them lies against the stockholder regularly receiving them); *O'Hare v. Marine Elec. Co.*, 229 Cal.App.2d 33, 36, 39 Cal. Rptr. 799, 800 (1964) (holding that where dividends are validly paid, recipients are not liable to anyone for their repayment, and if dividends are illegally paid, only the corporation may recover); cf. MINN. STAT. ANN. § 302A.557(1) (West 1985) (providing that a shareholder receiving an illegal distribution is liable to the corporation); N.D. CENT. CODE § 10-19.1-94(1) (1985) (providing that a shareholder who knows or should have known that they received an illegal distribution is liable to the corporation). See generally 9 B.E. WITKIN, SUMMARY OF CALIFORNIA LAW, *Corporations*, § 193 (9th ed. 1989) (discussing the liability of shareholders to corporations involving unlawful dividends or purchases of shares).

4. See CAL. CORP. CODE § 164 (West 1990) (defining directors as neutral persons designated in the articles of incorporation as such or elected by the incorporators and natural persons designated, elected, or appointed by any other name or title to act as directors, and their successors).

5. *Id.* § 316(a) (amended by Chapter 1064); cf. MODEL BUSINESS CORP. ACT § 8.33 (1984) (providing that a director who votes for or assents to an illegal distribution is personally liable to the corporation). See generally 9 B.E. WITKIN, SUMMARY OF CALIFORNIA LAW, *Corporations*, § 109 (9th ed. 1989) (describing unauthorized distributions).

6. See CAL. CIV. CODE § 1430 (West 1982) (defining joint and several liability as an obligation that may be imposed upon several persons); see also BLACK'S LAW DICTIONARY 837 (6th ed. 1990) (defining joint and several liability as a liability in which the creditor may demand payment or sue one or more of the parties to such liability separately, or all of them together at the creditor's option).

7. CAL. CORP. CODE § 316(a) (amended by Chapter 1064); cf. ALA. CODE § 10-2A-75(a)(1) (1987) (providing that a director who votes for or assents to an illegal distribution of the assets of a corporation to its shareholders is jointly and severally liable to the corporation with all other directors so voting or assenting); MASS. GEN. LAWS ANN. ch. 156B, § 61 (West 1992) (providing that directors who vote to authorize any distribution to one or more of its stockholders will be jointly and severally liable to the corporation).

8. CAL. CORP. CODE §§ 316(d), 506(a) (amended by Chapter 1064).



corporation has adequate retained earnings that equal or exceed the proposed distribution.<sup>9</sup> Chapter 1064 adjusts the standards that must be met by a corporation that incurs obligations connected with the repurchase of its shares by requiring that all indebtedness incurred by the corporation in repurchasing shares must be added to retained earnings.<sup>10</sup>

Existing law provides that issuers and purchasers of debt securities<sup>11</sup> are exempt from the usury provisions of the California Constitution<sup>12</sup> if the security is issued in compliance with specific provisions.<sup>13</sup> Chapter 1064 extends the usury exemption currently granted to debt securities issued with initial corporate offerings to debt securities issued in connection with any reorganization<sup>14</sup> or recapitalization.<sup>15</sup>

#### INTERPRETIVE COMMENT

Chapter 1064 was enacted to explain that if a shareholder or a director is civilly liable for an illegal noncash distribution, the value of the property distributed is the fair market value of the property at the time of the illegal distribution plus accrued interest.<sup>16</sup> Additionally, Chapter 1064 was enacted to clarify that a corporation must debit retained earnings for all indebtedness incurred by the corporation for the repurchases of its shares.<sup>17</sup> Finally, Chapter 1064 extends the usury exemption currently belonging to initial corporate offerings to securities issued for any recapitalization and reorganization.<sup>18</sup>

*Lisa R. Brenner*

---

9. *Id.* § 500 (amended by Chapter 1064).

10. *Id.* § 500(d) (amended by Chapter 1064).

11. *See* CAL. FIN. CODE § 5105.8 (West 1989) (defining corporate debt security as a marketable obligation evidencing the indebtedness of any corporation in the form of a bond, note, or debenture, or both note and debenture, which is commonly regarded as a debt security and is not predominately speculative in nature).

12. *See* CAL. CONST. art. 15, § 1 (setting forth California usury laws).

13. CAL. CORP. CODE § 25116 (amended by Chapter 1064); *see id.* (listing the specific provisions that must be followed to exempt issuers and purchasers of debt securities from California's usury provisions as a qualification under Chapter 2 (commencing with § 25120) or Chapter 3 of the California Corporations Code).

14. *See* BLACK'S LAW DICTIONARY 1298 (6th ed. 1990) (defining reorganization as an act or process of organizing again or anew).

15. CAL. CORP. CODE § 25116 (amended by Chapter 1064); *see* BLACK'S LAW DICTIONARY 1267 (6th ed. 1990) (defining recapitalization as a process whereby stock, bonds, or other securities of a corporation are adjusted or restructured as to type, amount, income, or priority).

16. ASSEMBLY FLOOR, COMMITTEE ANALYSIS OF AB 3649, at 1-2 (May 31, 1994).

17. *Id.* at 2.

18. *Id.*

**Business Associations and Professions; immigration consultants—bonding requirements**

Business and Professions Code §§ 22443.1, 22447 (new and repealed);  
§ 22443 (amended).  
AB 3137 (Escutia); 1994 STAT. Ch. 562

Existing law regulates immigration consultants<sup>1</sup> by providing that it is a misdemeanor<sup>2</sup> for them to perform various fraudulent acts in the course of providing their services.<sup>3</sup> Second and subsequent offenses may result in incarceration in a state prison.<sup>4</sup>

Chapter 562 adds to the regulation of immigration consultants the requirement that they file either a \$10,000 bond or cash deposit with the Secretary of State<sup>5</sup> who is authorized to hold the deposit for two years following the depositor's cessation of activities as an immigration consultant.<sup>6</sup> Damages awarded in a

---

1. See CAL. BUS. & PROF. CODE § 22441 (West 1987) (defining immigration consultant as one who gives advice on any proceeding, filing, or action regarding immigration or citizenship).

2. See CAL. PENAL CODE § 17(a) (West Supp. 1994) (defining a misdemeanor as a crime or public offense not classified as a felony or as an infraction); see also *id.* § 19 (West 1988) (providing that misdemeanors are punishable by imprisonment in the county jail not to exceed six months, by fine not to exceed \$1000, or both).

3. CAL. BUS. & PROF. CODE § 22440 (West 1987); see *id.* (providing that it is unlawful for anyone other than a lawyer or one authorized by federal law to represent persons before the Board of Immigration Appeals or the United States Immigration and Naturalization Service (INS)); see also *id.* § 22444 (West Supp. 1994) (providing that it is unlawful for immigration consultants to make false or misleading statements to clients, to make guarantees to clients that are unwritten or without basis in fact, to make statements that the consultant can or will obtain special favors or can exercise special influence with the INS, or to charge fees to refer clients to another that will perform services that the consultant cannot or will not provide); *id.* § 22445 (West Supp. 1994) (providing that a violation of the code sections pertaining to immigration consultants constitutes a misdemeanor and is punishable by a fine of \$1000 to \$2000 per client or up to one year in prison or both). See generally, Robert W. Lucas, Review of Selected 1987 Legislation, *Business Associations and Professions; Immigration Consultants*, 19 PAC. L.J. 427, 477 (1988) (discussing existing law regarding the duties of immigration consultants).

4. CAL. BUS. & PROF. CODE § 22445 (West Supp. 1994).

5. See CAL. GOV'T CODE §§ 12150-12172.5 (West 1992) (defining the office and duties of the Secretary of State).

6. CAL. BUS. & PROF. CODE § 22443.1 (enacted by Chapter 562); see *id.* § 22443.1(a), (h) (enacted by Chapter 562) (providing for the filing of a bond or deposit with the Secretary of State by immigration consultants and excluding from the requirement employees of nonprofit, tax-exempt corporations helping immigration applicants complete required forms provided their fees, if any, are consistent with those authorized by the INS and reflect the reasonable costs of the corporation); see also *id.* § 22443.1(c) (enacted by Chapter 562) (requiring the Secretary of State to charge a filing fee to defray the cost of filing the bond or deposit provided for in AB 3137); *id.* § 22443.1(b) (enacted by Chapter 562) (requiring the bond required by AB 3137 to be held for the benefit of persons damaged by fraud, misstatement, misrepresentation, unlawful act or omission, or failure to provide the services of the immigration consultant); *id.* § 22443.1(e)-(f) (enacted by Chapter 562) (providing for the payment of a deposit in lieu of the bond required in California Business and Professions Code § 22443.1(a), which may be retained by the Secretary of State for two years after the date on which the payer has ceased to act as an immigration consultant).

proceeding for injuries resulting from the acts of an immigration consultant may be recovered from the bond or cash deposit required by Chapter 562.<sup>7</sup>

Existing law additionally prohibits immigration consultants from retaining clients' original documentation.<sup>8</sup> Chapter 562 retains this prohibition, but additionally requires immigration consultants to retain copies of all client documents for at least three years after providing services and requires consultants to provide clients with copies of all documents or forms completed on their behalf.<sup>9</sup>

#### INTERPRETIVE COMMENT

Chapter 562 was enacted to augment existing law protecting clients from unscrupulous immigration consultants and was prompted by a proliferation of claims regarding instances of unfair or fraudulent practices.<sup>10</sup> Authors of Chapter 562 sought to address recent reported incidents where victims have been: Overcharged, charged without receiving services, charged for fraudulent documents, or fraudulently charged for legal services or special influence with the INS.<sup>11</sup>

---

7. CAL. GOV'T CODE § 22447(a) (enacted by Chapter 562); *see id.* § 22447(b) (enacted by Chapter 562) (providing that when there has been a recovery against a bond or cash deposit, the immigration consultant must file a new bond or deposit sufficient to cover claims up to \$10,000 and may not conduct business unless and until the new bond or deposit has been filed); *see also id.* § 22443.1(e) (enacted by Chapter 562) (requiring that one asserting a claim against a deposit must establish the claim by furnishing evidence to the Secretary of State of a money judgment entered by a court along with evidence that the claimant is entitled to recover damages from a bond or cash deposit under California Business and Professions Code § 22447); *id.* § 22443.1(h) (enacted by Chapter 562) (exempting from the requirements of AB 3137, employees of nonprofit, tax-exempt corporations who help clients complete application forms in immigration matters). *But see id.* § 22443.1(i) (enacted by Chapter 562) (maintaining the effectiveness of these provisions only until January 1, 1998).

8. CAL. BUS. & PROF. CODE § 22443(b) (amended by Chapter 562).

9. *Id.* § 22443(a) (enacted by Chapter 562).

10. SENATE COMMITTEE ON BUSINESS AND PROFESSIONS, COMMITTEE ANALYSIS OF AB 3137, at 3 (June 27, 1994); *see id.* (citing the proliferation of fraudulent schemes by immigration consultants as the impetus behind AB 3137); *see also* SENATE JUDICIARY COMMITTEE, COMMITTEE ANALYSIS OF AB 2520, at 3 (June 28, 1994) (citing the intent behind a piece of similar legislation to curb abuses of consumers by immigration consultants while preserving the services offered by honest consultants); Telephone Interview with Richard Garcia, Executive Director, California Rural Legal Assistance Foundation (July 18, 1994) (copy on file with the *Pacific Law Journal*) (stating that the California Rural Legal Assistance Foundation (CRLA) receives more than 500 calls per month over its Fresno hotline reporting incidences of abuses by immigration consultants).

11. SENATE COMMITTEE ON BUSINESS AND PROFESSIONS, COMMITTEE ANALYSIS OF AB 3137, at 3 (June 27, 1994); *see* Susan Freinkel, *Filipina's Suit Depicts Web of Deceit; Illegal Alien Risks Deportation to Pursue Consultant and Attorneys for \$4,500*, THE RECORDER, Sept. 25, 1992, at 1 (reporting cases in which immigration consultants collect fees and then disappear or file for bankruptcy); *see also* Deborah Sontag, *Aspiring Immigrants Misled on Chances in Visa Lottery*, N.Y. TIMES, June 20, 1994, at A1, A12 (citing cases of fraudulent promises by immigration consultants to provide "special secrets" purportedly allowing clients to obtain green cards through the lottery); Deborah Sontag, *You Don't Need a Tout for This Race*, INT'L HERALD TRIB., June 21, 1994, at 1 (reporting cases of unscrupulous immigration consultants charging clients for special advantages in the visa lottery, a system by which eligible immigrants are randomly granted green cards); Jose Velez, U.S. NEWS & WORLD REP., Apr. 18, 1994, at 23 (reporting an incident where an immigration consultant was indicted on charges that he collected millions of dollars by filing falsified amnesty

Chapter 562 seeks to curb abuses in an underregulated field by providing enforcement weapons, such as the \$10,000 bond or deposit requirement, to assist in collection from insolvent defendants, and the document retention requirement to assist consumers in claims against consultants.<sup>12</sup>

*Mark W. Owens*

**Business Associations and Professions; investments in South Africa—  
indemnification of costs**

Government Code § 7514 (amended).  
AB 2237 (McDonald); 1994 STAT. Ch. 46

Government Code §§ 12261, 12262, 12263, 12264, 12265, 12266, 12267, 12269 (repealed); §§ 16640, 16641, 16641.5, 16641.6, 16642, 16642.5, 16642.7, 16643, 16644, 16645, 16646, 16647, 16648, 16649, 16649.5 (repealed and new); § 15364.21 (amended); Public Utilities Code §§ 8276, 8277, 8278, 8279 (amended).  
AB 2448 (Brown); 1994 STAT. Ch. 31  
(*Effective March 30, 1994*)

Prior law imposed economic sanctions on South Africa by prohibiting, with some exceptions, the investment of state trust fund money in businesses or financial institutions that conduct business with South Africa.<sup>1</sup> Prior law further prohibited the California State World Trade Commission from providing assistance and information to the government of South Africa, and all corporations in California had to disclose whether or not they conduct any

---

applications for Asian illegal aliens); *Immigration Consultant Faces Charge*, TORONTO STAR, June 3, 1994, at A22 (reporting an incident in which a Croatian couple were fraudulently charged \$5400 to bring the couple's parents out of a Serbian dominated area of Bosnia by an immigration consultant). *See generally* Deborah Sontag, *Aspiring Immigrants Misled on Chances in Visa Lottery*, N.Y. TIMES, June 20, 1994, at A1, A12 (explaining the visa lottery system).

12. Stephen Rosenbaum, Statement in Support of AB 3137 (June 27, 1994) (copy on file with the *Pacific Law Journal*); *see* Caitlin Rother, *Migrants Victimized by Green Card Scams*, SAN DIEGO UNION-TRIB., Mar. 23, 1994, at A1 (citing concerns that the lack of regulation of immigration consultants reduces the likelihood that authorities will apprehend wrongdoers).

---

1. 1993 Cal. Legis. Serv. ch. 440, sec. 1, at 2057 (enacting CAL. GOV'T CODE § 7514); 1986 Cal. Stat. ch. 1254 sec. 2, at 4389 (enacting CAL. GOV'T CODE § 16641); *see* SENATE FLOOR, COMMITTEE ANALYSIS OF AB 2237, at 1 (Apr. 4, 1994) (discussing the extent of California state and local public retirement system investment in bonds guaranteed by foreign governments); *cf.* 22 U.S.C.A. §§ 5001-5117 (West Supp. 1994) (outlining the Federal government's Comprehensive Anti-Apartheid Act).

business with South Africa.<sup>2</sup> Further, the California Public Utilities Commission was required to exclude any losses incurred from investment of retirement funds in the government of South Africa from its operating budget.<sup>3</sup>

Chapter 46 repeals these sanctions.<sup>4</sup> Chapter 31 also provides for the indemnification of all costs incurred because of business operations in South Africa or decisions not to invest in business operations in South Africa.<sup>5</sup> In addition, Chapter 31 provides for indemnification to the Regents of the University of California for lost investment opportunities in South Africa.<sup>6</sup>

#### INTERPRETIVE COMMENT

Many restrictions were placed on South Africa due to outrage at its apartheid policies.<sup>7</sup> In 1986, the University of California Board of Regents voted to divest

---

2. The People's Right to Know Act, Prop. 105, § 3 (codified at CAL. GOV'T CODE § 12262); see ASSEMBLY FLOOR, COMMITTEE ANALYSIS OF AB 2448, at 1 (Mar. 21, 1994) (discussing the requirements of disclosing South Africa connections in a company's prospectus). *But see* Chemical Specialties Mfrs. Ass'n, Inc. v. Deukmejian, 227 Cal. App. 3d 663, 670, 278 Cal. Rptr. 128, 132 (1991) (prohibiting the implementation of disclosure requirements under Proposition 105, passed by California voters on November 9, 1988, because they are not functionally related to the objectives of the enactment and violate California's constitutional requirement limiting ballot measures to a single subject); see also CAL. CONST. art. II, § 8(d) (defining California's single-subject rule). See generally Philip Hager, *Court Rejects 'Truth-In-Ads' Ballot Measure*, L.A. TIMES, Feb. 12, 1991, at A1 (providing an account of the *Chemical Specialties* decision).

3. 1992 Cal. Legis. Serv. ch. 546 sec. 1, at 1729 (amending CAL. PUB. UTIL. CODE § 3276); see *id.* sec. 2 at 1729 (amending CAL. PUB. UTIL. CODE § 8277) (requiring companies to submit a list of investments in South Africa to the California Public Utilities Commission (CPUC)); *id.* sec. 3 at 1729 (amending CAL. PUB. UTIL. CODE § 8278) (allowing the PUC to verify investment information); *id.* sec. 4 at 1729 (amending CAL. PUB. UTIL. CODE § 8279) (allowing this section to be applied to additional countries).

4. Compare 1993 Cal. Legis. Serv. ch. 440 sec. 1, at 2057 (enacting CAL. GOV'T CODE § 7514) and 1992 Cal. Legis. Serv. ch. 546 sec. 1, at 1729 (amending CAL. PUB. UTIL. CODE § 8276) and *id.* sec. 2 at 1729 (amending CAL. PUB. UTIL. CODE § 8277) with CAL. GOV'T CODE § 7514 (amended by Chapter 46) and CAL. PUB. UTIL. CODE § 8276 (amended by Chapter 31) (representing the dichotomy between the old and the new law); see also ASSEMBLY FLOOR, COMMITTEE ANALYSIS OF AB 2448, at 1 (Mar. 21, 1994) (contrasting California's prior policy on South Africa with the changes implemented by Chapter 46); SENATE FLOOR, COMMITTEE ANALYSIS OF AB 2237, at 1 (Apr. 4, 1994) (discussing the addition of South Africa to the list of countries in which public retirement systems may invest).

5. CAL. GOV'T CODE § 16640 (repealed and enacted by Chapter 31); see also ASSEMBLY FLOOR, COMMITTEE ANALYSIS OF AB 2448, at 2 (Mar. 21, 1994) (discussing indemnification from the California General Fund for all claims, demands, suits, actions, damages, or judgments resulting from business losses from South African investments).

6. CAL. GOV'T CODE § 16641 (enacted by Chapter 31); see ASSEMBLY FLOOR, COMMITTEE ANALYSIS OF AB 2448, at 2 (Mar. 21, 1994) (discussing the specific requirement that all employees of the University of California be compensated as provided under California Government Code § 16640).

7. Howard N. Fenton, III, *The Fallacy of Federalism in Foreign Affairs: State and Local Foreign Policy Trade Restrictions*, 13 J. INT'L. L. BUS. 563, 564 (1993); see *id.* (discussing the use of economic sanctions as weapons of choice in the maintenance of international order); see also *id.* at 577 (maintaining a \$20 billion value of assets subject to some form of state and local divestment law in the United States, as of 1993). See generally George Church, *Apartheid's New Upheaval; As Black Townships Simmer, Divestiture Divides the U.S.*, TIME, July 22, 1985, at 34 (describing South African unrest and the reaction of the United States public and law-making bodies).

all investments with ties to South Africa.<sup>8</sup> Later that same year, the California Legislature followed the lead of many other states by divesting state trust fund monies, as well as restricting banks from lending to South African concerns.<sup>9</sup> Total California divestment was to be complete by January 1, 1991.<sup>10</sup> Further, California public utilities were precluded from including any losses from South African investments in their budgets.<sup>11</sup>

The impetus for Chapters 31 and 46 was Nelson Mandela's election to President of South Africa, and his United Nations plea on September 24, 1993 for world communities to lift sanctions against his country.<sup>12</sup> For the first time, South Africa will be led by a black majority.<sup>13</sup> President Clinton echoed Mandela's plea, calling on both the several states and the Federal Government to end restrictions on trade and investment.<sup>14</sup>

---

8. WILLIAM F. MOSES, A GUIDE TO AMERICAN STATE AND LOCAL LAWS ON SOUTH AFRICA 1 (1992); see *id.* at 1, 13-14 (discussing the University of California policy concerning South Africa adopted in 1986); cf. Matthew Countryman, *Beyond Victory: Lessons of the Divestment Drive; Influence of Student Movements on Social Change*, THE NATION, Mar. 26, 1988, at 406 (discussing the student movement and the ensuing divestment response at various universities); *At Last, A Campus Cause*, THE ECONOMIST, Apr. 12, 1986, at 32 (describing anti-apartheid campaigns at Harvard and other university campuses in 1986).

9. 1993 Cal. Legis. Serv. ch. 440 sec. 1, at 2057 (enacting CAL. GOV'T CODE § 7514); 1986 Cal. Stat. ch. 1255, sec. 1, at 4391-92 (enacting CAL. PUB. UTIL. CODE §§ 8276-79); see Board of Trustees of the Employees' Retirement System of Baltimore v. Mayor and City Council of Baltimore, 562 A.2d 720, 725 (Md. 1989), *cert. denied sub nom.* Lubman v. Mayor and City Council of Baltimore City, 493 U.S. 1093 (1990) (upholding the constitutionality of Baltimore's divestment law); cf. ILL. ANN. STAT. ch. 40, para. 5/1-110 (Smith-Hurd 1993) (prohibiting any new investments in South Africa after Feb. 1, 1987); LA. REV. STAT. ANN. § 308.2 (West 1987) (restricting the state treasurer from depositing state funds in any financial institution with ties to South Africa); ME. REV. STAT. ANN. tit. 5, § 1951 (West 1989) (prohibiting state funds to be deposited in any institution with loans to South Africa, or being invested in companies with ties to South Africa); MD. CODE ANN., STATE FIN. & PROC. § 6-208 (1988) (restricting bank deposits); MICH. COMP. LAWS ANN. § 23(1)(d)(ii) (West 1994) (prohibiting investments in banks which have loans to any corporation that manufactures military supplies for use in South Africa); N.J. STAT. ANN. § 52:18A-89.1 (West 1986) (restricting bank deposits); 1994 MO. LEGIS. SERV. 105.686 (Vernon). *But see* Regents of the University of Michigan v. State, 419 N.W.2d 773, 780 (Mich. App. 1988) (finding Michigan's divestment law to violate that state's constitution).

10. 1986 Cal. Stat. ch. 1254, sec. 2 at 4390 (enacting CAL. GOV'T CODE § 16644). See generally MOSES, *supra* note 8, at 13 (discussing California and other states approaches to divesting public funds from South African concerns).

11. 1992 Cal. Legis. Serv. ch. 546 sec. 1, at 1729 (amending CAL. PUB. UTIL. CODE § 8276); *id.* sec. 2 at 1729 (amending CAL. PUB. UTIL. CODE § 8277); *id.* sec. 3 at 1729 (amending CAL. PUB. UTIL. CODE § 8278); *id.* sec. 4 at 1729 (amending CAL. PUB. UTIL. CODE § 8279).

12. SENATE COMMITTEE ON PUBLIC EMPLOYMENT AND RETIREMENT, COMMITTEE ANALYSIS OF AB 2448, at 3 (Mar. 7, 1994); see *Transition in Africa; Mandela Calls to an End to Sanctions*, N.Y. TIMES, Sept. 25, 1993 at 1 (providing the text of Mandela's United Nations address).

13. Bruce W. Nelan, *Time to Take Charge; At Long Last, the Black Majority Moves From Repression Into the Halls of Government*, TIME, May 9, 1994, at 27; see *id.* (chronicling South Africa's history of leadership, and discussing the impact of that country's first all-race elections).

14. Stanley Meisler, *Mandela Calls for End of South African Sanctions; Leader of ANC Cites Democratic Advances, Says Lifting Curbs Will Aid Stability, Progress; Clinton Urges Swift Action; Arms Embargo Would Remain for Now*, L.A. TIMES, Sept. 25, 1993, at A1; see *id.* (discussing President Clinton's call to lift sanctions, and the upcoming trade mission to South Africa).

Chapters 31 and 46 are expected to have a substantial effect on the Public Employees' Retirement System investments, as businesses reenter South Africa.<sup>15</sup> Other states and municipalities, as well as universities have already lifted their anti-apartheid sanctions.<sup>16</sup> Military armaments, however, are still under a mandatory United Nations embargo.<sup>17</sup>

*Timothy M. Harris*

## **Business Associations and Professions; licenses to sell alcoholic beverages**

Business and Professions Code § 23958.4 (new); § 23958 (amended).  
AB 2897 (Caldera); 1994 STAT. Ch. 630

Under existing law, the Department of Alcoholic Beverage Control (Department)<sup>1</sup> issues licenses<sup>2</sup> to qualified applicants to sell<sup>3</sup> alcoholic beverages.<sup>4</sup> Under prior law, the Department could deny a license to an otherwise qualified applicant if granting a license would have tended to create a law enforcement problem or would have resulted in or added to an undue concentration of licenses.<sup>5</sup> Chapter 630 requires the Department to deny an application that tends

---

15. SENATE FLOOR, COMMITTEE ANALYSIS OF AB 2448, Mar. 14, 1994, at 2; *see id.* (listing the Public Employees' Retirement System (PERS) as a supporter of Chapter 31); *see also* SENATE FLOOR, COMMITTEE ANALYSIS OF AB 2237, at 2 (Apr. 4, 1994) (discussing PERS investment requirements, and the effect of the new laws).

16. *Mandela Asks End to Boycott; In Swift Response, Senate Approves Bill Lifting Sanctions; Clinton Plans Appeal to Cities and States*, S.F. EXAMINER, Sept. 24, 1993, at A1; *cf.* OR. REV. CODE 293.830, 293.867(2) (West 1991) (representing the first state to restrict sanctions against South Africa). *See generally* *Colleges Reverse Divestment Plans*, N.Y. TIMES, Nov. 28, 1993, at A33 (discussing Howard University's, Wesleyan University's, and Connecticut College's approach to amending their divestment policies); *U.S. Businesses Awaiting Resolution of Issues Before Return to South Africa*, WALL ST. J., Mar. 23, 1992, at A8 (discussing the reticence of U.S. corporations to reenter South African concerns).

17. *U.N. Economic Curbs on Pretoria Are Lifted*, N.Y. TIMES, Oct. 8, 1994, at A8; *see id.* (discussing the history of U.N. sanctions and the mandatory arms embargo).

---

1. *See* CAL. BUS. & PROF. CODE § 23050 (West 1985) (establishing the Department of Alcoholic Beverage Control in the executive branch of state government).

2. *See id.* § 23320 (West Supp. 1994) (listing the types of licenses to sell alcoholic beverages).

3. *See id.* § 23025 (West 1985) (defining sell and sale to include any transaction in which title to alcoholic beverage is transferred from one person to another for any consideration).

4. *Id.* § 23958 (amended by Chapter 630); *see* CAL. CONST. art. XX, § 22 (giving the exclusive power to the Department of Alcoholic Beverage Control to grant, deny, suspend, or revoke licenses to manufacture, import, or sell alcoholic beverages in California); CAL. BUS. & PROF. CODE § 23004 (West 1985) (defining alcoholic beverage as including anything that is fit for drinking that contains more than one-half of one percent alcohol by volume).

5. 1982 Cal. Stat. ch. 1189, sec. 2, at 4244 (amending CAL. BUS. & PROF. CODE § 23958); *see* Department of Alcoholic Beverage Control v. Alcoholic Beverage Control Appeals Bd., 122 Cal. App. 3d 549, 557 n.6, 175 Cal. Rptr. 342, 346 n.6 (1981) (characterizing cases, where a law enforcement problem was found, as involving repeated or ongoing criminal conduct of a legitimate and substantial concern to law enforcement).

to create a law enforcement problem or causes or adds to an undue concentration of licenses.<sup>6</sup> However, Chapter 630 continues to permit the Department to issue a license upon a showing that public convenience or necessity would be served by the issuance.<sup>7</sup>

Existing regulatory law defines undue concentration as an application for a license in a crime reporting district with a twenty percent higher-than-average crime rate compared to all the crime reporting districts of the local law enforcement agency, and a higher-than-average ratio of retail licenses to population in the applicant's census tract or district as compared to the ratio for the applicant's county.<sup>8</sup> Chapter 630 codifies the regulatory definition of undue concentration but also alters it to mean either a twenty percent higher-than-average crime rate or a higher-than-average ratio of licenses to population.<sup>9</sup> For all but a few retail licenses, Chapter 630 also grants authority to the local governing body of the area in which the premises would be located to determine whether public convenience or necessity would be served by the issuance of a license.<sup>10</sup>

---

agencies); *id.* at 556-57, 175 Cal. Rptr. at 345-46 (holding that an expectation that disturbances of undetermined severity would sometimes occur at the Marmalade Max Disco in the indefinite future was insufficient as grounds for finding a law enforcement problem); *see also* Kirby v. Alcoholic Beverage Control Appeals Bd., 7 Cal. 3d 433, 437-39, 498 P.2d 1105, 1107-09, 102 Cal. Rptr. 857, 860-61 (1972) (finding a law enforcement problem where an off-sale beer and wine license would have been located in a village at the edge of a university campus where the crime rate was 50-60% higher than the rest of county and where civil disturbances had been occurring); Harris v. Alcoholic Beverage Control Appeals Bd., 212 Cal. App. 2d 106, 114, 28 Cal. Rptr. 74, 78-79 (1963) (finding a revocation of license justified due to a law enforcement problem where the testimony of two police officers indicated that intoxicated persons were arrested at the establishment at a rate of seven to eight per week); Torres v. Department of Alcoholic Beverage Control, 192 Cal. App. 2d 541, 546, 13 Cal. Rptr. 531, 535 (1961) (finding a denial of license justified at an establishment in an area where 75 arrests per month were made for public drunkenness).

6. CAL. BUS. & PROF. CODE § 23958 (amended by Chapter 630).

7. *Id.* § 23958.4(b) (enacted by Chapter 630); *see* Sepatis v. Alcoholic Beverage Control Appeals Bd., 110 Cal. App. 3d 93, 102-03, 167 Cal. Rptr. 729, 734-35 (1980) (holding that the Department of Alcoholic Beverage Control acted within its discretion to determine public convenience when it approved a license for a "fern" bar, despite overconcentration, based in part on testimony that such a bar would appeal to some people presently reluctant to enter other bars in the vicinity). *But cf. id.* at 100, 167 Cal. Rptr. at 733 (discussing, without explicitly rejecting, the Alcoholic Beverage Control Appeals Board's reasoning that determining public convenience or necessity on the basis of expressed preferences of association could involve impermissible accommodation of social prejudices).

8. CAL. CODE REGS. tit. 4, § 61.3 (1994); *see id.* (defining undue concentration).

9. CAL. BUS. & PROF. CODE § 23958.4(a)(1)-(3) (enacted by Chapter 630).

10. *Id.* § 23958.4(b)(2) (enacted by Chapter 630); *see* SENATE FLOOR, COMMITTEE ANALYSIS OF AB 1082, at 2 (Aug. 12, 1994) (asserting that the bill allows a local government to make the determination that public necessity would be served by the issuance of the license). *But cf. id.* (suggesting, without reference to authority, that prior to AB 2897, the license applicant, rather than the Department of Alcoholic Beverage Control, made the determination of public necessity). Chapter 630 codifies the regulatory scheme, whereby the Department of Alcoholic Beverage Control alone determines public convenience or necessity for nonretail licenses, retail licenses in bona fide eating places or in lodging establishments, and licenses issued in conjunction with a beer manufacturer's or a winegrower's license. CAL. BUS. & PROF. CODE § 23958.4(b)(1) (enacted by Chapter 630); *see id.* § 23012 (West 1985) (defining beer manufacturer as any person engaged in the manufacture of beer); *id.* § 23013 (West 1985) (defining winegrower as any person with the equipment for converting grapes into wine and is engaged in the production of wine, except for persons producing 200 gallons or less per year for solely personal consumption); *id.* § 23038 (West 1985) (defining bona fide eating place as



# INTERPRETIVE COMMENT

Chapter 630 is intended to make it more difficult to obtain most retail licenses to sell alcoholic beverages in areas impacted by an overconcentration of alcohol outlets.<sup>11</sup> The bill mandates, with exceptions, the denial of permits in areas of overconcentration.<sup>12</sup> However, by altering the definition of undue concentration, Chapter 630 has lost a key element of the regulatory scheme.<sup>13</sup> Previously, undue concentration was achieved by satisfying two specified requirements; under Chapter 630, undue concentration may be achieved by satisfying either one of the requirements.<sup>14</sup> Chapter 630 would produce the curious result, for example, in a county where the licenses are evenly distributed among the census tracts that *any* new retail license *anywhere* in the county would cause what is defined under Chapter 630 to be an undue concentration.<sup>15</sup> Also, in shifting power from the Department of Alcoholic Beverage Control to the local governing body, Chapter 630 may violate the California Constitution which

---

one regularly kept open for the serving of meals to guests for compensation with a sanitary kitchen and proper refrigeration space); *id.* § 23356 (West 1985) (listing rights and obligations of beer manufacturers and winegrowers); *id.* § 23357 (West Supp. 1994) (listing terms under which a beer manufacturer may sell beer).

11. ASSEMBLY FLOOR, COMMITTEE ANALYSIS OF AB 2897, at 2 (May 26, 1994); *see id.* (stating that the bill mandates, rather than permits, the denial of a retail license in area with undue concentration of licenses while admitting that AB 2897 also provides exceptions to the mandate).

12. CAL. BUS. & PROF. CODE § 23958 (amended by Chapter 630); *see* AB 2897, 1993-1994 Calif. Leg. Reg. Sess. § 1 (Apr. 4, 1994) (mandating, in an earlier version of AB 2897, the denial of permits without any exceptions, in areas of overconcentration).

13. CAL. BUS. & PROF. CODE § 23958.4(a)(3) (enacted by Chapter 630); *see id.* (defining undue concentration as a census tract or division where the ratio of off-sale retail licenses to population exceeds the countywide average). This definition of undue concentration does not require any reference to the crime rate in the area. *Id.*; *see also* Kirby v. Alcoholic Beverage Control Appeals Bd., 71 Cal. 2d 1200, 1205, 459 P.2d 657, 661, 81 Cal. Rptr. 241, 245 (1969) (limiting the power of the Legislature over the licensing activities of the Department of Alcoholic Beverage Control under the California Constitution to reasonable control of the Department's discretion); Department of Alcoholic Beverage Control v. Kolender, 136 Cal. App. 3d 315, 319, 186 Cal. Rptr. 189, 191 (1982) (finding the existing regulatory scheme reasonable because it analyzes both the number of licenses per population and the crime rate); *cf.* Linda L. Munden, Comment, *Retail Liquor Licenses and Due Process: The Creation of Property Through Regulation*, 32 EMORY L.J. 1199, 1239 (1983) (asserting that, because a liquor license is treated as property under California law, courts extend a high degree of due process in the regulation of these licenses).

14. Compare CAL. CODE REGS. tit. 4, § 61.3 (1994) (requiring both a higher than average crime rate and a higher than average ratio of licenses to population for a finding of undue concentration) with CAL. BUS. & PROF. CODE § 23958.4(a)(1)-(3) (enacted by Chapter 630) (requiring either a higher than average crime rate or a higher than average ratio of licenses to population for a finding of undue concentration).

15. CAL. BUS. & PROF. CODE § 23958.4(a)(3) (enacted by Chapter 630); *see supra* note 13 (defining undue concentration).

places power exclusively in the state government to license the sale of alcoholic beverages within the state.<sup>16</sup>

*Owen W. Dukelow*

**Business Associations and Professions; limited liability companies**

Business and Professions Code §§ 16602.5, 17901.5 (new); §§ 17900, 17902, 17910.5, 17913, 17914 (amended); Commercial Code § 3307 (amended); Corporations Code §§ 161.7, 167.3, 167.7, 167.8, 171.03, 171.07, 171.3, 174.5, 190.7, 17000, 17001, 17002, 17003, 17004, 17005, 17050, 17051, 17052, 17053, 17054, 17055, 17056, 17057, 17058, 17059, 17060, 17061, 17062, 17100, 17101, 17102, 17103, 17104, 17105, 17106, 17107, 17150, 17151, 17152, 17153, 17154, 17155, 17156, 17157, 17158, 17200, 17201, 17202, 17250, 17251, 17252, 17253, 17254, 17255, 17300, 17301, 17302, 17303, 17304, 17350, 17351, 17352, 17353, 17354, 17355, 17356, 17357, 17450, 17451, 17452, 17453, 17454, 17455, 17456, 17457, 17500, 17501, 17550, 17551, 17552, 17553, 17554, 17555, 17556, 17600, 17601, 17602, 17603, 17604, 17605, 17606, 17607, 17608, 17609, 17610, 17611, 17612, 17613, 17650, 17651, 17652, 17653, 17654, 17655, 17700, 17701, 17702, 17703, 17704, 17705, (new); §§ 161, 190, 1109, 1113, 1201, 15046, 15611, 15632, 15678.2, 25013, 25019 (amended); Financial Code § 1220 (amended); Government Code § 12164.7 (new); §§ 8670.3, 12185 (amended); Health and Safety Code §§ 25118, 25281 (amended); Penal Code §§ 387, 653s (amended); Public Resources Code § 40170 (amended); Revenue and Taxation Code § 28 (repealed); §§ 28.5, 17087.6, 18633.5, 23305.5, 23091, 23092, 23093, 23094, 23095, 23096 (new); §§ 19, 64, 480, 480.1, 480.2, 6005, 6829, 7310, 8606, 11204, 17007, 17220, 18402, 18535, 18621.5, 18637, 18638, 18648, 19002, 19009, 19132, 19254, 23036, 23038, 25141, 30010, 38106, 40004, 41003, 43006, 45006, 46020, 55002

---

16. CAL. CONST. art. XX, § 22; *see id.* (providing that the State has the exclusive right and power to license and regulate the manufacture, sale, purchase, possession, and transportation of alcoholic beverages within the State); *Korean Am. Legal Advocacy Found. v. City of Los Angeles*, 23 Cal. App. 4th 376, 385, 28 Cal. Rptr. 2d 530, 536 (1994) (stating that an ordinance regulating the sale of alcoholic beverages would be preempted by the state constitution), *review denied*, 1994 Cal. LEXIS 3928 (1994); *City of Rancho Cucamonga v. Warner Consulting Services, Ltd.*, 213 Cal. App. 3d 1338, 1344-45, 262 Cal. Rptr. 349, 353 (1989) (holding that the regulation of liquor licenses is not within the general police power of local entities granted by Article XI, section 7 of the California Constitution because Article XX, section 22 carves out a special exception to that general police power), *review denied*, 1989 Cal. LEXIS 5040 (1989); *see also* CAL. CONST. art. XI, § 7 (granting power to counties and cities to make and enforce within its limits all local, police, sanitary, and other ordinances not in conflict with general laws). *But cf. Korean Am. Legal Advocacy Found.*, at 389, 28 Cal. Rptr. at 538 (upholding a city ordinance that may have some indirect impact on the sale of alcoholic beverages as a valid exercise of power to control and abate nuisances). *See generally* Thomas B. Griffen, Note, *Zoning Away the Evils of Alcohol*, 61 S. CAL. L. REV. 1373, 1385 (1988) (arguing that it is difficult to determine the scope of the preemption by state law of local regulation of alcoholic beverages).

(amended); Unemployment Insurance Code §§ 125.4, 135, 135.1, 610, 1116, 1735, 2071, 2107, 2109, 2110, 2110.3, 2110.5, 2110.7, 13005 (amended); Vehicle Code § 675 (amended).  
SB 469 (Beverly) 1994 STAT. Ch. 1200  
(Effective September 30, 1994)

Existing law provides for the formation of partnerships,<sup>1</sup> corporations,<sup>2</sup> and unincorporated associations.<sup>3</sup> Chapter 1200 authorizes the creation of an additional business entity—the limited liability company (LLC).<sup>4</sup>

---

1. See CAL. CORP. CODE § 15611 (West Supp. 1994) (defining partnership); *id.* §§ 15001-15800 (West 1991 & Supp. 1994) (setting forth the provisions for co-owners of a business for profit under the Uniform Partnership act); see also *Industrial Asphalt, Inc. v. State Bd. of Equalization*, 5 Cal. App. 4th 1237, 1240, 7 Cal. Rptr. 2d 444, 446 (1992) (holding that a transferor of assets to a partnership remains liable for obligations assumed by the partnership regardless of whether any stipulation is made so establishing). See generally *Wescott v. Gilman* 170 Cal. 562, 566, 150 P. 777, 781 (1915) (laying out the necessary steps for forming a partnership, as reflected in the California Corporations Code); 9 B.E. WITKIN, SUMMARY OF CALIFORNIA LAW, *Partnerships*, §§ 22-30 (9th ed. 1989) (describing the requirements for the formation of a partnership).

2. See CAL. CORP. CODE § 167 (West 1990) (defining domestic corporation); see also *id.* §§ 101-2260 (West 1990 & Supp. 1994) (detailing provisions for the formation, powers, limitations, and liability of a general corporation). See generally 9 B.E. WITKIN, SUMMARY OF CALIFORNIA LAW, *Corporations*, §§ 63-80 (9th ed. 1989) (setting forth the requirements for forming a corporation in California).

3. CAL. CORP. CODE §§ 21000-24007 (West 1991 & Supp. 1994); see *id.* (providing for the formation and liability of various nonprofit associations, including medical associations and real estate investment trusts).

4. *Id.* § 17050 (enacted by Chapter 1200). Forty-three states have already enacted legislation allowing for LLC's. ASSEMBLY JUDICIARY COMMITTEE, COMMITTEE ANALYSIS OF SB 469, at 1 (June 29, 1994). See e.g. COLO. REV. STAT. ANN. §§ 7-80-101-7-80-913 (West 1994), DEL. CODE ANN. tit. 6, §§ 18-101-18-913 (1994), FLA. STAT. ANN. §§ 608.401-608.471 (West Supp. 1994), GA. CODE ANN. §§ 14-11-100-14-11-1108 (Supp. 1994), ILL. ANN. STAT. ch. 805, para. 180/1-1-ch. 805, para. 180/1-160 (Smith-Hurd Supp. 1994), IOWA CODE ANN. §§ 490A.100-490A.1601 (West Supp. 1994), MD. CODE ANN., CORPS. & ASSN'S §§ 4A-101-4A-1103 (1994), R.I. GEN. LAWS §§ 7-16-1-7-16-75 (1994), TEX. REV. CIV. STAT. ANN. art. 1528n.1.01-1528n.9.12 (West Supp. 1994), VA. CODE ANN. §§ 13.1-1000-13.1-1073 (Michie 1994), W. VA. CODE §§ 31-1A-1-31-1A-69 (1992), WYO. STAT. §§ 17-15-101-7-15-136 (1989) (providing for the formation, management and liability of domestic and foreign limited liability companies); cf. Daniel B. Moskowitz, *New Ways to Organize Business is Gaining Wider Acceptance*, WASH. POST, Nov. 4, 1991, at 14 (discussing the evolution of the LLC in the United States); John Schmeltzer, *Illinois Lawmakers OK Creation of 'Limited Liability Company'*, CHI. TRIB., June 30, 1992, at 4 (discussing Illinois' LLC law and the arguments for and against it); David Young, *New Liability Options for Small Firms Here*, CHI. TRIB., Mar. 25, 1993, at 1 (comparing "S" corporation law in Illinois and the new LLC law). See generally Marybeth Bosko, *The Best of Both Worlds: The Limited Liability Company*, 54 OHIO ST. L.J. 175 (1993) (discussing LLC laws of other countries, as well as the advantages of domestic LLC laws); Susan Pace Hamil, *The Limited Liability Company: A Possible Choice for Doing Business?*, 41 FLA. L. REV. 721 (1989) (discussing the classification of LLC's as partnerships for federal income taxation purposes and discussing the business situations in which the use of an LLC might be advantageous); Richard M. Horwood & Jeffrey A. Hechtman, *The Better Alternative: The Limited Liability Company*, 20 J. REAL EST. TAX'N 348 (1993) (discussing the tax aspects of an LLC as well as the statutory formation requirements); Robert R. Keating et al., *The Limited Liability Company: A Study of the Emerging Entity*, 47 BUS. LAW. 378 (1992) (providing a history, discussion of the characteristics, comparison with other business forms, comparison of eight existing statutes, discussion of federal income tax ramifications, explanation of member limited liability in intrastate and interstate transactions, and a discussion of the evolving uses of LLC's); Larry E. Ribstein, *Limited Liability and Theories of the Corporation*, 50 MD. L. REV. 80 (1991) (discussing different legal viewpoints and the impact of LLCs).

FORMATION AND STRUCTURE

Under Chapter 1200, an LLC may be formed by any two persons, who may be an individual, corporation, partnership, or another LLC.<sup>5</sup> Persons interested in forming an LLC must file articles of organization with the Secretary of State.<sup>6</sup> A statement must also be filed yearly that includes, *inter alia*, the purpose of the LLC and the names of managing members.<sup>7</sup> An LLC under Chapter 1200, however, may not provide professional services.<sup>8</sup>

Limited Liability Company members<sup>9</sup> may be assigned different classes with various rights, powers, and duties.<sup>10</sup> However, each member of the LLC is responsible for its management, unless otherwise specified in the articles of organization.<sup>11</sup> Managers<sup>12</sup> have the same fiduciary duty to the LLC and its members that a partner owes to a partnership and to other partners.<sup>13</sup> Additionally, a written agreement may allow the appointment of officers who may or may not be members of the LLC.<sup>14</sup> If more than one manager is appointed, all decisions must be made by a majority vote of the managers.<sup>15</sup>

Members may contribute capital to the LLC, and profits and losses are to be distributed among members in proportion to the members' contributions unless the operating agreement specifies otherwise.<sup>16</sup>

Before doing business in California, foreign LLCs must register with the Secretary of State, or be subject to a fine.<sup>17</sup> Foreign LLCs will be governed by the

---

5. CAL. CORP. CODE § 17050 (enacted by Chapter 1200); SENATE RULES COMMITTEE, ANALYSIS OF SB 469, at 2 (Jan. 27, 1994).

6. CAL. CORP. CODE § 17050 (enacted by Chapter 1200).

7. *Id.* §§ 17050-17062 (enacted by Chapter 1200).

8. 1994 Cal. Legis. Serv. ch. 1200, sec. 93, at 6103; *see* CAL. CORP. CODE § 13401(a) (West 1991 & Supp. 1994) (defining professional services); *see also* SENATE FLOOR, COMMITTEE ANALYSIS OF SB 469, at 2 (Jan. 27, 1994) (providing that permission to form an LLC will not be extended to an organization requiring licensing, certification, or registration under the Business and Professions Code or the Chiropractic Act).

9. *See* CAL. CORP. CODE § 17100 (enacted by Chapter 1200) (defining membership for LLC purposes); *id.* § 17101(b) (enacted by Chapter 1200); *cf.* *Hester Int'l Corp. v. Federal Republic of Nigeria*, 879 F.2d 170 (1989) (discussing piercing the corporate veil of an LLC incorporated under Nigerian law); *Abu-Nassar v. Elders Futures, Inc.*, 1991 U.S. Dist. LEXIS 3794 (1991) (discussing piercing the corporate veil of an LLC organized under Lebanese law).

10. CAL. CORP. CODE § 17102-17103 (enacted by Chapter 1200).

11. *Id.* § 17150 (enacted by Chapter 1200); *see id.* § 17151(b) (enacted by Chapter 1200) (listing the circumstances when the names of managers are required to be contained in an LLC's articles of organization).

12. *See* CAL. CORP. CODE §§ 17150-17158 (enacted by Chapter 1200) (discussing the status and requirements of LLC management).

13. *Id.* § 17153 (enacted by Chapter 1200). *See generally* B. Troy Villa, *The Status of Enforcing Fiduciary Duties in a Limited Partnership*, 49 LA. L. REV. 1217 (1989) (describing the duties owed by general partners to a limited partnership); Steven A. Waters, *Partnerships*, 47 SMU L. REV. 1483, 1487 (1994) (describing the current state of the law with regard to the discharge of partner liability after dissolution).

14. CAL. CORP. CODE § 17154(a) (enacted by Chapter 1200).

15. *Id.* § 17156 (enacted by Chapter 1200). If management is vested in only one member, the articles of organization must so state. *Id.* § 17151(b).

16. *Id.* § 17202 (enacted by Chapter 1200).

17. *Id.* § 17451 (enacted by Chapter 1200); *id.* § 17456(b) (enacted by Chapter 1200); *see id.* (setting the fine for noncompliance at \$20 per day, up to a maximum of \$10,000).

laws of the state in which they are organized.<sup>18</sup> Foreign LLCs will not be denied California registration simply because their home states' laws differ.<sup>19</sup>

Like a corporation, LLC members may bring actions against the LLC to assert a common claim.<sup>20</sup> In response, the LLC may file a motion compelling the suing class to post security in order to proceed with their action.<sup>21</sup>

Chapter 1200 permits LLCs to be merged with other business entities.<sup>22</sup> Any reorganization, including mergers, must address objections of dissenting members.<sup>23</sup>

### LIABILITY

Existing law specifies that shareholders of a corporation will generally only be held liable for judgments against the corporation to the extent of their capital contributions or par value of the stock.<sup>24</sup> Partners may be subject to unlimited liability for debts of a partnership.<sup>25</sup>

Members of an LLC will not be subject to personal liability for a judgment, debt, or other obligation of the LLC, whether the liability or obligation arises from contract, tort, or otherwise.<sup>26</sup> Members are only responsible to the extent that shareholders in a corporations would be liable.<sup>27</sup>

### TAX RAMIFICATIONS

Under existing law, corporations doing business<sup>28</sup> in California are subject to a 9.3% tax on net income.<sup>29</sup> A 1.5% net income tax is imposed on Subchapter S<sup>30</sup>

---

18. *Id.* § 17450(a) (enacted by Chapter 1200); *see* Keating, et al., *supra* note 4, at 394 (discussing generally the treatment of foreign LLC's in various states); SENATE COMMITTEE ON REVENUE AND TAXATION, COMMITTEE ANALYSIS OF SB 469, at 2 (Jan. 5, 1994) (stating that foreign LLCs will be treated as partnerships, and thus not subject to California's 9.3% corporation tax).

19. CAL. CORP. CODE § 17450(b) (enacted by Chapter 1200).

20. *Id.* §§ 17500-17501 (enacted by Chapter 1200).

21. *Id.* § 17501(c) (enacted by Chapter 1200).

22. *Id.* §§ 17550-17556 (enacted by Chapter 1200).

23. *Id.* §§ 17600-17613 (enacted by Chapter 1200); *see* SENATE JUDICIARY COMMITTEE, ANALYSIS OF SB 469, at 9 (Jan. 4, 1994) (stating that dissenting LLC members have rights substantially similar to those provided to limited partners).

24. CAL. CORP CODE § 414(a) (West 1990); *see id.* (providing that no action shall be brought against shareholders of a corporation, unless a creditor has an unsatisfied judgment against the corporation, or if such proceedings would be useless).

25. *Id.* § 15015 (West 1991).

26. *Id.* § 17101(a) (enacted by Chapter 1200).

27. *Id.* § 17101(b) (enacted by Chapter 1200).

28. *See* CAL. REV. & TAX CODE § 23101 (West 1992) (defining doing business).

29. *Id.* § 24341 (West 1992); *see id.* (defining net income); *id.* § 23151 (West 1992) (setting the tax rate at 9.3 % for fiscal years ending in 1987 and thereafter).

30. *See* I.R.C. § 1362(s) (1986) (discussing the federal tax ramifications for Subchapter S corporations); CAL. REV. & TAX CODE § 23801 (West 1992 & Supp. 1994) (discussing the requirements for formation and termination of a Subchapter S corporation); *see also id.* § 23802 (West 1992 & Supp. 1994) (discussing generally the tax treatment of Subchapter S corporations). *See generally* Edward J. Roche, Jr. et al., *Limited*

corporations.<sup>31</sup> No tax based on income is imposed on limited partnerships.<sup>32</sup> All three entities, however, are subject to a minimum tax of \$800.<sup>33</sup>

Partnerships and proprietorships, under existing law, are not subject to such an entity-level tax.<sup>34</sup> The owners of these types of businesses, however, are subject to income tax as profits are earned.<sup>35</sup> Under Chapter 1200, an LLC will generally be treated like a partnership for tax purposes.<sup>36</sup> Further, LLCs are required to file partnership tax returns.<sup>37</sup> Unlike a partnership, however, LLCs will be subject to the \$800 minimum corporate tax, in addition to a special fee which will vary depending on income.<sup>38</sup>

#### INTERPRETIVE COMMENT

Chapter 1200 was enacted to make California a more competitive business environment.<sup>39</sup> Currently, 43 states have enacted some sort of LLC provisions.<sup>40</sup>

---

*Liability Companies Offer Pass-Through Benefits Without S Corp. Restrictions*, 74 J. TAX'N 248 (1991) (discussing the differences between LLCs and S corporations).

31. CAL. REV. & TAX CODE § 23802 (West Supp. 1994); *see id.* (setting the tax rate at 1.5% for Subchapter S Corporations).

32. *Id.* § 23081 (West 1992 & Supp. 1994); *see id.* (subjecting limited partnerships to only those taxes described in California Revenue and Taxation Code § 23153-a franchise tax of at least \$800).

33. *Id.* § 23153(d)(1) (West 1992 & Supp. 1994); *see id.* (setting a minimum tax of \$800 for all corporations subject to California Revenue and Taxation Code § 23151); *see also id.* § 23081(b) (West 1992) (defining limited partnership for tax purposes); SENATE COMMITTEE ON REVENUE AND TAXATION, COMMITTEE ANALYSIS OF SB 469, at 1 (Jan. 5, 1994) (discussing the tax structure for partnerships, limited partnerships, and corporations under existing law). The LLC has the same minimum tax as a corporation in California. *Id.*

34. SENATE COMMITTEE ON REVENUE AND TAXATION, COMMITTEE ANALYSIS OF SB 469, at 1 (Jan. 5, 1994).

35. *Id.*

36. CAL. REV. & TAX. CODE §§ 23091(a)-(d), 23092(a)-(d) (enacted by Chapter 1200); *see* Sheldon I. Banoff et al., *Tax Trap for Professionals Forming LLCs*, 79 J. TAX'N 63, 64 (1993) (discussing the disadvantages of LLCs and partnerships for professional organizations).

37. CAL. REV. & TAX. CODE § 23091(a) (enacted by Chapter 1200); *see* SENATE COMMITTEE ON REVENUE AND TAXATION, COMMITTEE ANALYSIS OF SB 469, at 2 (Jan. 5, 1994) (discussing the parallels between partnerships and LLCs).

38. CAL. REV. & TAX CODE § 23092(a) (enacted by Chapter 1200).

39. SENATE RULES COMMITTEE, COMMITTEE ANALYSIS OF SB 469, at 4 (Jan. 27, 1994); Norman D. Williams, *New Law is a Friend to Business*, SACRAMENTO BEE, Oct. 4, 1994, at F1; *see id.* (citing a number of business chambers and organizations predicting "the law will light a fire under business startups in the state," and that the LLC is a particularly good vehicle for businesses that are just starting out because of the tax advantages, simplicity of formation, and few limitations as opposed to other business entities); *State Developments, California*, DAILY REP. FOR EXECUTIVES (BNA) Aug. 26, 1994, at 164 (confirming that California needed LLC legislation to remain competitive with other states already having such laws).

40. ASSEMBLY JUDICIARY COMMITTEE, COMMITTEE ANALYSIS OF SB 469, at 1 (June 29, 1994); *see supra* note 4 (providing examples of others states' LLC laws).

Granting a small or medium sized business entity LLC status results in considerable federal and state tax savings for that organization, coupled with limited liability.<sup>41</sup>

Partnership tax treatment for LLCs comes from LLCs' having only two of the four "corporate characteristics" as defined by the Internal Revenue Service (IRS).<sup>42</sup>

Limited Liability Companies are simpler and more flexible than Subchapter S corporations or limited partnerships.<sup>43</sup> They combine a corporation's liability protections with the tax advantages of a partnership.<sup>44</sup> LLCs are analogous to a general partnership where the partners have no personal liability, to a limited partnership with no general partner, or to a partnership surrounded by a corporate shell.<sup>45</sup>

Proponents of Chapter 1200 expect the flexibility LLCs offer will attract new businesses and create jobs in California.<sup>46</sup> As California was lacking LLC legislation, it was feared that small businesses would organize elsewhere.<sup>47</sup>

Critics of Chapter 1200 are concerned with a potential loss of tax revenue from small businesses and a proliferation of liability-free organizations.<sup>48</sup> Others worry

---

41. SENATE COMMITTEE ON REVENUE AND TAXATION, COMMITTEE ANALYSIS OF SB 469, at 2 (Jan. 5, 1994); see *Williams*, *supra* note 40 (discussing the benefits of LLCs and their tax advantages over both corporations and partnerships).

42. Rev. Rul. 88-76, 1988-2 C.B. 360; see *id.* (classifying a Wyoming LLC for purposes of federal taxation using the four "corporate characteristics" test); see also SENATE COMMITTEE ON REVENUE AND TAXATION, COMMITTEE ANALYSIS OF SB 469, at 2 (Jan. 5, 1994) (describing the four "corporate characteristics": (1) Continuity of life; (2) centralized management; (3) limited liability; and (4) free transferability of ownership interest); see *id.* (stating that any LLC with limited liability and one other characteristic passes the IRS test). See generally William R. Culp & John Joseph Carpenter, *IRS Pronouncements Clarify Status as Partnership vs. an Association*, 6 J.PARTNERSHIP TAX'N 111, 112 (1989) (discussing the four corporate characteristics for tax purposes); Robert D. Howard, *Partnership Rulings Eased by New Limited Liability, Net Worth Tests*, 70 J. TAX'N 334, 335 (1989) (criticizing the IRS test for determining the classification of an entity for purposes of federal income taxation).

43. Thomas Scheffey, *Limited Liability, Unlimited Possibilities*, CONN. LAW TRIB., Apr. 19, 1994, at 1; see Bob Sanders, *Hybrid of Corporation, Partnership Called Limited Liability Company*, N.H. BUS. REV., May 14, 1993, at 1 (discussing the simplicity of LLCs as compared to other common forms of business plans); Witner & Simons, *Tax Aspects of Limited Liability Companies*, 63 CPA J. 22 (1993) (stating that LLCs are subject to more liberal tax rules and are free from the eligibility restrictions that mark S corporations, as they may be part of an affiliated group, have more than 35 shareholders, and have more than one class of stock as well as having a corporation as a shareholder).

44. Witner & Simons, *supra* note 43, at 22

45. *Id.*; see *id.* at 25 (discussing the differences between an LLC and a limited partnership: with an LLC, every member has limited liability, and can participate in management decisions).

46. SENATE FLOOR, COMMITTEE ANALYSIS OF SB 469, at 2 (Jan. 27, 1994).

47. *Id.*; see *Williams*, *supra* note 39 (discussing the expansion of LLC legislation encompassing a majority of states).

48. SENATE COMMITTEE ON REVENUE AND TAXATION, COMMITTEE ANALYSIS OF SB 469, at 4 (Jan. 5, 1994); see *id.* (quoting New York Tax Commissioner James Wetzer as saying "The federal government has opened up a candy store. New York businesses ought to be able to shop at the candy store. But we in our present budget situation cannot afford to subsidize their purchase of this federal candy"); SENATE JUDICIARY COMMITTEE, ANALYSIS OF SB 469, at 3 (Jan. 4, 1994) (expressing concern that insurance requirements covered under SB 469 would be inadequate to protect contract and tort judgment creditors against undercapitalized LLCs). But see *Use of Limited Liability Companies Seen Not Jeopardizing Corporate Tax Base*, BNA MGMT. BRIEFING, Mar. 30, 1993, at 1 (citing the reports of several practitioners that the use of LLCs will not erode

about untested problems with a new business entity and do not see the LLC as offering anything unavailable with corporations, limited partnerships, or Subchapter S corporations.<sup>49</sup>

In response to critics' fears that doctors and lawyers would forego malpractice insurance in favor of LLC status, professional organizations are not allowed to enjoy LLC status under Chapter 1200.<sup>50</sup>

*Timothy M. Harris*

## **Business Associations and Professions; weights and measures—violations**

Business and Professions Code § 12015.3 (repealed and new); §§ 12015.5, 12028 (new); §§ 12003, 12240 (amended).  
SB 1644 (Kelley); 1994 STAT. Ch. 592

Existing law provides that a county sealer<sup>1</sup> who has knowledge of violations of the California Code governing weights and measures<sup>2</sup> must see that the violator is prosecuted by the district attorney.<sup>3</sup> Chapter 592 authorizes the sealer, after providing a warning, to levy a civil penalty of up to \$1000 in addition to investigation costs for each violation and provides that payment of the penalty

---

the corporate tax base).

49. Sanders, *supra* note 44, at 1; *see id.* (arguing that LLCs are nothing more than the latest fad to beat corporate taxes, and that state security offices would be unable to keep up with this new type of entity, leading to litigation because of a variety of unsolved issues); *id.* (stating that limited partnerships with a corporate general partner provides the same benefits that an LLC does); *Partnerships, Final Subchapter K Rules Will Include More Safe Harbor Examples, Official Says*, DAILY REP. FOR EXECUTIVES, Nov. 1, 1994, at 209 (discussing the confusion that may result in treating real estate rental interests held as a limited liability member).

50. SENATE JUDICIARY COMMITTEE, ANALYSIS OF SB 469, at 3 (Jan. 4, 1994); *see id.* (stating that professional organizations had originally been included in SB 469, but opposition from the California Trial Lawyers Association led to exclusion based on fears that attorneys who commit malpractice would be deterred from settling disputes because they could escape liability by forming an LLC); *id.* (substantiating such fears through examples of large settlements obtained from firms that had represented Lincoln Savings and Loan Association, where large settlements were obtained from firms providing representation; if those firms had been organized as LLCs, those settlements may have been impossible); *id.* (outlining similar fears with regard to doctors, accountants, and dentists who may escape liability for their negligent behavior).

---

1. *See* CAL. BUS. & PROF. CODE § 12008 (West 1987) (providing that the term sealer, for the purposes of weights and measures, is used to refer to the State Sealer and county sealers); *see also id.* § 12004 (West 1987) (defining the State Sealer as the chief of the State Department of Agriculture charged with enforcement of the code division regarding weights and measures); *id.* § 12006 (West 1987) (defining county sealer as any sealer appointed by the county); *id.* § 12200 (West 1987) (establishing the office of the county sealer of weights and measures); *id.* § 12209 (West 1987) (defining the duties of the county sealer).

2. *See id.* §§ 12001-13741 (West 1987 & Supp. 1994) (containing the code division governing weights and measures).

3. *Id.* § 12015 (West 1987).



will constitute a complete defense to a criminal prosecution for the violation.<sup>4</sup> The revenues derived from civil penalties levied under Chapter 592 are to be deposited in the Department of Food and Agriculture Fund<sup>5</sup> to be used by the State Sealer to carry out his or her duties under the code sections pertaining to weights and measures.<sup>6</sup>

Chapter 592 additionally requires the State Sealer or county sealer to provide all reports and records regarding actions taken against violators within the last four months following a written request of the state Attorney General or district attorney in his or her district.<sup>7</sup> Chapter 592 excludes from its scope violations involving utility meters in mobile home parks, recreational vehicle parks, or apartment complexes where the owner of the park or complex is responsible for utility meters.<sup>8</sup> These provisions of Chapter 592 will become effective thirty days after specified regulations are adopted by the Secretary of Food and Agriculture and will remain in effect for two years thereafter.<sup>9</sup>

Existing law also requires various registration fees<sup>10</sup> for weighing and measuring devices while, among other things, setting maximum annual registration charges not to exceed the county's actual inspection and testing costs, exempting motortruck scales from a fee of \$200 for weighing devices with capacities of 20,000 pounds or more, and exempting farm milk tanks from all annual registration fees.<sup>11</sup> Chapter 592 instead limits annual registration charges to the amounts specified in the Table of Maximum Annual Charges<sup>12</sup> and removes

---

4. *Id.* § 12015.3(a)-(b) (repealed and enacted by Chapter 592); *see id.* (providing for notification of proposed actions against violators and providing for the means and content of such notices); *see also id.* § 12015.3(b)-(d) (repealed and enacted by Chapter 592) (providing for the right of any person charged and notified of a proposed action against him or her under Chapter 592 to a hearing and providing for notification of the time and place of the hearing, for the rules governing the hearing, for the filing of appeals, and for the rendering of decisions); *id.* § 12015.5 (enacted by Chapter 592) (providing that any person convicted of a violation of the laws pertaining to weights and measures or determined to be civilly liable under Chapter 592 will be liable for reasonable investigation costs incurred by the sealer); *id.* § 12028 (enacted by Chapter 592) (requiring the Department of Food and Agriculture to specify the types of violations subject to civil penalties by July 1, 1995 as well as the amounts of penalties for each violation and the procedure for providing notice to persons charged).

5. *See* CAL. FOOD & AGRIC. CODE § 221 (West Supp. 1994) (establishing the Department of Food and Agriculture Fund and providing for receipts to and disbursements from the fund).

6. CAL. BUS. & PROF. CODE § 12015.3(e) (repealed and enacted by Chapter 592).

7. *Id.* § 12015.3(g) (repealed and enacted by Chapter 592).

8. *Id.* § 12015.3(f) (repealed and enacted by Chapter 592).

9. *Id.* § 12015.3(h) (repealed and enacted by Chapter 592); *see id.* § 12028 (enacted by Chapter 592) (requiring the Secretary of State to adopt regulations specifying the types of violations for which civil penalties may be imposed pursuant to California Business and Professions Code § 12015.3, the amounts of these penalties, subject to specified requirements, and a procedure for providing notice to persons charged with violations).

10. *See id.* § 12240(a) (amended by Chapter 592) (establishing annual device registration fees to recover inspection and testing costs).

11. *Id.* § 12240 (amended by Chapter 592).

12. *See id.* § 12240(f) (amended by Chapter 592) (providing the maximum annual charge per location that may be assessed based on the number of devices to be inspected or tested at each location).

the exemption for motortruck scales, but limits the annual charge for these instruments as well as livestock scales to \$100 per device.<sup>13</sup>

#### INTERPRETIVE COMMENT

Chapter 592 was enacted to enable local governments with limited financial resources to maintain the quality of weighing and measuring instrument<sup>14</sup> inspections.<sup>15</sup> The continued ability to accurately and frequently inspect these devices is intended to protect consumers from unfair charges for commodities whose prices are based on the weight or measurement of the goods sold.<sup>16</sup>

Chapter 592 was also intended to facilitate the use of the administrative hearing process as an alternative to criminal prosecution which provides that a violation of the law of weights and measures constitutes a misdemeanor.<sup>17</sup>

Chapter 592 also addresses the vagueness of existing law which fails to establish whether the county board of supervisors must set device registration charges for instruments with capacities of 20,000 pounds or more.<sup>18</sup>

*Mark W. Owens*

---

13. *Id.* § 12240 (amended by Chapter 592); *see id.* § 12240(i) (amended by Chapter 592) (providing for a \$100 registration fee for motortruck scales); *see also id.* § 12240(l) (amended by Chapter 592) (adding livestock scales to those devices subject to a \$100 registration fee and limiting the fee to \$100 per location provided there are no more than three such devices at a single location).

14. *See id.* § 12500(a) (West Supp. 1994) (defining weighing instrument as any device, contrivance, apparatus, or instrument to be used for ascertaining weight and defining measuring instrument as any device, contrivance, apparatus, or instrument to be used for ascertaining measure).

15. ASSEMBLY COMMITTEE ON LOCAL GOVERNMENT, COMMITTEE ANALYSIS OF SB 1644, at 3 (June 29, 1994); *see id.* (citing the fiscal crises of local governments and lack of resources to pursue violators as the impetus for enactment of Chapter 592); *see also id.* (stating that Chapter 592 resulted from a collaboration among industry representatives, the California District Attorney's Association, and the California Agricultural Commissioners and Sealers Association).

16. *See Pitney-Bowes, Inc. v. State*, 108 Cal. App. 3d 307, 321, 166 Cal. Rptr. 489, 498 (1980) (stating the legislative intent behind the Business and Professions Code sections governing weights and measures as the protection of consumers from unfair dealings due to inaccurate weighing); *see also SENATE FLOOR, COMMITTEE ANALYSIS OF AB 1491*, at 1-2 (Sept. 3, 1993) (citing the purpose behind a similar bill to ensure adequate funding of county sealer inspections and quoting a statement made by representatives of Los Angeles County that only one third of all cases of overcharging by weighing and measuring instrument operators are actually prosecuted).

17. CAL. BUS. & PROF. CODE § 12015.3(c) (repealed and enacted by Chapter 592); *see id.* (providing for oral arguments, decision, and appeal processes presided over by the Secretary of Food and Agriculture); *see also id.* § 12510 (West Supp. 1994) (listing and defining the violations of the code pertaining to weights and measures that constitute misdemeanors); ASSEMBLY COMMITTEE ON LOCAL GOVERNMENT, COMMITTEE ANALYSIS OF SB 1644, at 3 (June 29, 1994) (citing the desire to avoid court backlogs while still providing for uniform and equitable application of the law).

18. CAL. BUS. & PROF. CODE § 12240 (amended by Chapter 592); *see ASSEMBLY COMMITTEE ON LOCAL GOVERNMENT, COMMITTEE ANALYSIS OF SB 1644*, at 3 (June 29, 1994) (stating that the Table of Maximum Annual Charges provided the limits for device registration charges, but that it was unclear whether the county board of supervisors could use this table to set fees for vehicles weighing 20,000 pounds or more).

